Summer 2019

At the Hands of Fate: The Political Economy of Islamic Insurance in Indonesia, Malaysia, and Pakistan, C. 1980 to the Present

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A Dissertation Submitted to the Faculty of
Old Dominion University in Partial Fulfillment of the
Requirements for the Degree of

DOCTOR OF PHILOSOPHY

INTERNATIONAL STUDIES

OLD DOMINION UNIVERSITY
August 2019

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ABSTRACT

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Why have Islamic insurance systems developed well in some countries, but not in others? Malaysia is considered as Islamic insurance elite due to its relatively large number of operators it houses as well as the sustained growth of Islamic insurance sales within the country, while Indonesia and Pakistan are still in early stages of development. Analyzing the political and social history of Islamization of insurance systems in these three Muslim majority countries in Asia since 1980s, this dissertation demonstrates the development gap between these countries on Islamic insurance results from; firstly, complex bargains made between various groups within each country polity, and those bargains are structured by the country's fundamental political institutions. Secondly, the gap is also an outcome of different societal transformations during the Islamization that 'produce Islam(s)' in these countries. The revival of Islamic principles in these countries does not only create Sharia-compliant financial products but produces Islamic norms, identities, ethics, and practices enacted in their risk management.

This dissertation is dedicated to my beloved wife, Aini.

ACKNOWLEDGMENTS

Throughout the writing of this dissertation I have received a great deal of support from many people and various organizations. I extend my special thanks to my advisor, Dr. Francis Adams for his patience and encouragement that have helped this project to develop in significant ways. Dr. David Earnest also provided invaluable support to me, particularly in the initial phase of this project. I am very appreciative of his thoughtfulness that led me to explore many aspects of the topic. Also, my committee would have been incomplete if it were not for the contribution of Dr. David Selover.

A very special gratitude goes out to all down at the Institute of International Education (IIE) and AMINEF for helping and providing the funding of a Fulbright scholarship, the Dean Office of the College of Arts and Letters, ODU for giving assistantship during the dissertation process, and President University, Indonesia for the continuous support throughout my 'sabbatical' from the university.

Also, my dissertation has been enriched by my participation in training opportunities provided by the International Institute of Islamic Thought (IIIT). Special thanks to Dr. Ermin Sinanovic, for pointing me to a body of scholarship and connecting me to scholar networks outside my discipline that have greatly enhanced my work. Through IIIT, I had the privilege to embark on a novel intellectual journey with great support from the professors, staff and my fellow students of SSP 2016. Finally, I need to thank my fellow GPIS students, the American and International friends of GSF, Indonesian community of Virginia Beach, and brothers and sisters of the Muslim community of Tidewater for their hospitality. Because of that, my family and I always feel that Hampton Roads is our second home.

GLOSSARY

Alim (pl. ulama): religious scholar in Islamic disciplines, gives opinions or issues rulings (fatwa) on religious questions

Bancatakaful: combination of Islamic banking with Islamic insurance

dawah: propagation of the Islamic faith

faqih (pl. *fuqaha*): a legal expert, jurist in Islamic law

fatwa (pl. *fatawat*): authoritative religious injunction without legal binding

fiqh: Islamic jurisprudence based upon the Quran and Sunnah

halal: that which is lawful, permitted, good, and praiseworthy in Islam

Hanafi school: one of the four religious Sunni Islamic schools of jurisprudence. It is named after the scholar Abu Hanifa an Nu'man ibn Thabit (d.767).

haram: actions that are unlawful and forbidden in Islam

hijab: clothing for the purposes of modesty and dignity according to Islamic dress code

ijtihad: independent reasoning. It is recognized as one of the legal methods of reasoning in Islamic law (Sharia), which is completely independent of any school (madhhab) of jurisprudence (fiqh).

madhhab (pl. madhahib): school of legal thought or jurisprudence that interpret the Quran and hadith for followers. There are four main madhahib; Hanafi, Maliki, Shafii, and Hanbali.

mudharabah: the commercial profit-sharing contract according to Islamic law

qadi: judge in the Islamic court system

pesantren: madrasah/traditional Islamic boarding school within Southeast Asian context

Shafii: one of the four religious Sunni schools of Islamic law. It was named after Imam al-Shafii who lived in the early 9th century.

Sharia: Islamic law

Sukuk: Islamic bonds

tajdid: renewal. In Islamic context, *tajdid* refers to the revival of Islam in order to purify and reform society.

Takaful: mutual guarantee. In the modern context, this term is used to name Islamic alternative for conventional insurance

riba: usury

ushr: specific type of religious tax implemented on agricultural products

wakalah: a principle in Islamic commercial law, which is based on the idea that the operator, acting as an agent of the participants, can charge its management expenses on the Islamic insurance contributions or premium paid.

zakat: religious tax, or obligatory distribution to the needy

zameen: Pakistani term for land, which along with family (zan) and wealth (zar) are the most important things to be protected according to the tribal law

zan: family

zar: wealth

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CHAPTER I

INTRODUCTION

Since the establishment of the first modern commercial Islamic bank, Dubai Islamic Bank (DIB) in 1975,1 Islamic financial instruments (IFIs) have been largely promoted as a panacea for many national economic problems, particularly throughout the Islamdom.[2] This initiative happened together with a growing common presumption that the economic development at that time was a secular project that needed a thorough reexamination. Iran, Malaysia, Pakistan, and Sudan led the way for a national program of establishing Islamic economy.

Furthermore, the Islamic finance market is a dynamic and rapidly expanding sector. IFIs are primarily comprised of Islamic Banking, *Sukuk* (Islamic Bonds), *Takaful* (Islamic insurance), and Islamic Mutual Funds.[3] Some scholars even argue these instruments help to maintain the stability of the financial system as a whole by the simple fact that it provides an alternative to the existing financial services. S. Nazim Ali and Shariq Nisar suggest, "The liberalization and globalization of the financial systems have led to a homogenized financial system with the same set of incentives and motivation, which led to global instability. Therefore, diversity in the structure is considered a stabilizing factor."[4] Scott Schmith, an international trade specialist at

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[1] Ibrahim Warde, *Islamic Finance in the Global Economy* (Edinburgh: Edinburgh University Press, 2000).

[2] A historian Marshall G.S. Hodgson introduced the term Islamdom and it refers to the society in which the Muslims and their faith are recognized as prevalent and socially dominant. He prefers not using the term Islamic world because this term implies there are many separate and mutually exclusive worlds. See detail discussion in Marshall G. S. Hodgson, *The Venture of Islam Conscience and History in a World Civilization* (Chicago: Chicago : University of Chicago Press, 1974). Page 58. For this dissertation, I will use term Islamdom to emphasize the transnational dimension and uniformity of Muslims beyond their local and national identity, and I will use 'Islamic societies' or Muslim societies talking about their diversity or particularities. Islamic societies and Muslim societies are used by another historian, Ira Lapidus, in his magisterial work Ira M. Lapidus, *A History of Islamic Societies*, 2nd ed.. ed. (Cambridge New York : Cambridge University Press, 2002); ibid.

[3] The word insurance or banking when prefixed by "Islamic‟ means that all theories and practices are examined from the perspective of Islamic laws and values as enshrined in the Quran (holy book) and Hadith (sayings of prophet Muhammad). See S. U Farooq et al., "An Analytical Study of the Potential of Takaful Companies," *European Journal of Economics Finance and Administrative Sciences* 20 (n.d.): 55–75.

[4] Finance Harvard University Forum on Islamic, *Takaful and Islamic Cooperative Finance : Challenges and Opportunities / Edited by S. Nazim Ali, Shariq Nisar*, *Studies in Islamic Finance, Accounting and Governance.* (Cheltenham, Glos ; Northampton, Massachusetts: Edward Elgar Publishing, 2016).

the International Trade Administration, Department of Commerce, USA, indicates other positive effects of Islamic finance. He shows in his report that the growth of Islamic finance has helped to diversify markets and institutional structures, particularly in oil-rich Muslim countries, and in countries with significant Muslim minorities.[5]

Furthermore, several studies confirm the role of Islamic-based economies in dealing with global financial crises. Studies conducted by the International Monetary Fund (IMF) show that co-operative banks-including local credit unions- and Islamic banks are among those financial institutions that survived the 2007-2008 economic crisis. They were relatively distant from 'speculative' financial market that made them more resilient to any financial shocks. Both institutions are different from commercial banks because they share some risk with the depositors.[6] During financial panics, Islamic banks especially were less prone to deposit withdrawals, but even so, their lending is consistently less sensitive to change in deposits. Therefore, during the recent crisis, these banks were able to provide more loans compared to commercial banks.[7]

Besides banking, another financial instrument that has gained prominence recently is *Takaful* or Islamic insurance. Takaful is a term for 'mutual guarantee' utilized by modern Muslim societies in times of economic insecurity- illness, unemployment, widowhood, old age, etc. Currently, Islamic insurance companies provide various Islamic insurance products such as life and family (i.e., education fund), medical, marine and aviation, property and accident, and auto insurances. Also, Islamic insurance has been used to unlock the potential for insurance penetration in the Islamdom. Insurance markets in this area are largely at nascent or growth stage of development with a very low insurance density, even in the most developed Muslim-majority countries.[8]

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[5] Scott Schmith, *Islamic Banking Experiencing Rapid Growth* (International Trade Administration, 2005), https://www.trade.gov/MAS/pdf/Islamic_Banking.pdf.

[6] Saeed Al-Muharrami and Daniel C Hardy, "Cooperative and Islamic Banks : What Can They Learn from Each Other?," *Working Paper No. 13/184* (2013), https://www.imf.org/en/Publications/WP/Issues/2016/12/31/Cooperative-and-Islamic-Banks-What-can-they-Learn-from-Each-Other-40888. Accessed September 20, 2016.

[7] Moazzam Farooq and Sajjad Zaheer, "Are Islamic Banks More Resilient During Financial Panics?" *IMF Working Paper Research Department and Strategy, Policy, and Review Department* (2015), https://www.imf.org/external/pubs/ft/wp/2015/wp1541.pdf (accessed September 20, 2016).

[8] Swiss Re sigma (2011), World Insurance (2010).

Islamic insurance has experienced substantial growth globally; however, there has been an uneven development of Islamic insurance between countries throughout the Islamdom. Some countries, such as Iran, Malaysia and Saudi Arabia are Islamic insurance elites due to their relatively large number of Islamic insurance operators their houses as well as the sustained growth of Islamic insurance sales within their countries, while others including Indonesia, Pakistan and Sudan are having limited development. This dissertation seeks to understand the factors that influence the different developments of Islamic insurance of the three most significant Islamic insurance markets in Asia: Indonesia, Malaysia, and Pakistan.

Islamic insurance: *fate, faith, and good faith*

The idea of insurance itself is a profoundly religious insight. We live in a world of uncertainty. We look around and still see potential disaster or risk at every turn. Illness, fire, earthquakes, economic slowdowns, global warming, terrorist threat shows that our ability to control our lives is not total. Religious scholars would say that in those big things, we are at the hands of fate or luck or God's will. We can be discipline exercising at the gym, eat healthy food and do not smoke to maintain our health. However, we have no control over healthcare cost. Insurance was designed with this awareness. It protects us from the powers beyond our control.[9]

Insurance works by enabling us to 'spread and transfer risk'. We pay a small amount of money regularly so-called premium to an insurance company to get protection when our time of need comes. Takaful or Islamic insurance goes beyond that. According to its proponents, Islamic insurance follows the principles of religious injunctions strictly. It is a risk-sharing arrangement based on Islamic law with a purpose to address the moral issues of speculation, interest-based practices, and financial exclusion of conventional insurance.

Takaful comes from an Arabic term *kafala* meaning 'cooperative' or mutual indemnity. It refers to the mutual assistance between members of society, be it a person, a society, an institution or a government. It came from a pre-Islamic Arab tribe's practice of giving blood money. It is argued by many Islamic scholars that Prophet Muhammad embraced and validated

[9] Steven Waldman, "Is the Health Insurance Industry Immoral?," *the Wall Street Journal*, August 5, 2009, accessed 13 October 2018, https://www.wsj.com/articles/SB124950683016308929.

it as part of the Islamic faith within the early Muslim society afterward.[10] Later, the Muslims used the concept of mutual assistance when they extended their trade by sea to the Far East. The merchants put aside a sum of money as a collective fund to compensate for any loss incurred by any of them during the trading journey.[11]

In the context of contemporary Islamic insurance, the initial official forum that discusses the legitimacy of insurance in the Islamic world was the Congress of Islamic Research in Cairo back in 1965. Afterward, at the first international conference on Islamic economics in 1976 in Mecca, Saudi Arabia, Islamic scholars from various countries met and reached a consensus that conventional insurance for profit was deemed as contradicting Islamic law.[12] In the early 1980s, Muslim scholars together with Muslim financial practitioners started to develop this concept as modern private-based insurance services where primarily a group of participants donating funds into a pool managed by a company that members could use in the event of personal or business contingencies.

The first Islamic insurance company -the Islamic Insurance Company of Sudan- was founded in Sudan in the year 1979. Another declaration was proclaimed in the Second Conference of International Council of *Fiqh* Academy of the Organization of the Islamic Conference (OIC) in Jeddah in 1985, which declared all forms commercial insurance is prohibited. [13] Also, this council recommended cooperative insurance as the preferred alternative.[14] Several countries followed it up by issuing specific Islamic insurance regulations, rules, and guidelines.

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[10] There were three kinds of mutual financial protection created by traditional Arab merchant: *hilf*, *daman khatr al-tarid* and *Aqila.* Hilf is mutual risk fund to assist victims of natural disasters or hazards of trade journeys. Daman khatr al-tariq (a kind of surety) was placed to recover the losses caused by bandits or pirates. Aqila was practiced preventing bloodshed among tribal members by extending compensation to ransom captives or to settle a claim from an accidental killing. For more detail, see: Abdullaah Jalil et al., *The Concept of Social Security in Islamic Economy*, *Islamic Economic System Conference 2015 (iECONS 2015)* (Krabi, Thailand: 2015).

[11] Syed Othman Alhabshi Shaikh Hamzah Shaikh Abdul Razak, "Takaful: Concept, History, Development, and Future Challenges of Its Industry," *Islam and Civilisational Renewal* 1, no. 2 (December 2009). https://www.icrjournal.org/icr/index.php/icr/article/view/268

[12] Muammar Dahnoun and Basil Alqudwa, "Islamic Insurance: An Alternative to Conventional Insurance," *American Journal of Humanities & Islamic Studies* 1, no. 1 (2018).

[13] The term 'commercial' was used before the establishment of Islamic bank and Islamic insurance. After the establishment, it is more common to use term 'conventional' Vis a vis 'Islamic' to differentiate the new method of Islamic commercial bank and Islamic commercial insurance and the common ways of banking and insurance.

[14] The Council of the Islamic Fiqh Academy, *Resolutions and Recommendations of the Council of the Islamic Fiqh Academy 1985-2000* (2012).

For example, after experimentation for more than a decade, Sudan promulgated a comprehensive Islamic insurance regulation in 1992, Pakistan replaced its old Insurance Act with the Insurance Ordinance in 2000, and Saudi Arabia enacted the new Supervision on Cooperative Insurance Act of 2003 and so on.[15] Before these regulations, Islamic insurance companies in those countries operated under conventional insurance or cooperative laws. Except for Malaysia, Islamic insurance companies in Malaysia started to run only after the promulgation of the Takaful Act of 1984.

Currently, there are two types of service provided by an Islamic insurance company: General Takaful and Family Takaful. General Takaful is usually a short-term policy where Islamic insurance participants pay contributions and operators undertake to manage risk. General Takaful gives protection to the participant for losses arising from perils such as accident, fire, flood, liability, and burglary. Family Takaful provides protection and long-term savings where participants or their beneficiary will be presented with financial benefits if they suffer a tragedy. At the same time, they will enjoy long-term personal savings because part of their contribution will be deposited in an account for savings. Participants will be able to enjoy investment returns from the savings portion based on a pre-agreed ratio.[16]

Nonetheless, there is no religious requirement for joining Islamic insurance. Not only Muslim but also everyone can use this service. Islamic insurance does not require the buyer to adhere to other Sharia principles within the religion of Islam or becomes a Muslim, but it only needs the buyer to comply with the Sharia or Islamic law principles of the conduct of business. Like conventional insurance the issues of "insurable interest" and *uberrimae fidei* (of the fullest confidence) are equally valid in Islamic insurance contract also. Islamic law emphasizes the principle of *uberrimae fidei* in any form of contractual agreement. According the Islamic jurists, the contract is void unless there is honesty, full disclosure, truthfulness, and utmost good faith

[15] Ajmal Bhatty and Shariq Nisar, "Takaful Journey: The Past, Present and Future," in *Takaful and Islamic Cooperative Finance: Challenges and Opportunities*, ed. S. Nazim Ali and Shariq Nisar (Cheltenham, UK: Edward Elgar Publishing, 2016).
[16] Dahnoun and Alqudwa.

among the parties. Non-compliance of these makes the contract unenforceable, and it applies fully to any Islamic insurance contract. [17]

Islamic scholars mention that the primary purpose of Islamic insurance is to deal with the prohibited or *haram* practices of modern finance: the payment of prohibited interest (*riba*), the existence of uncertainty in a transaction of inordinate risk and insufficient transparency (*gharar*), gambling (*maysir*), and investing in prohibited activities such as alcoholic beverage production, gambling, drugs and tobacco. It places great importance on the moral consequences of financial transactions. Besides that, Islamic insurance is different from other conventional finance in respect of risk mitigation. It uniquely emphasizes risk sharing rather than trading and shifting of risk. According to these scholars, Islamic insurance alters the practices of modern financial transactions in two ways: enforcing Sharia-compliant contracts and creating a mutual organizational framework.[18]

Sharia prohibits the use of the interest-based instrument and certain types of equities companies. According to Muslims' understanding, the use of interest creates possibilities of exploitation of the one who needs money by the one who has plenty. The basic premise of Islamic finance is the parties involved must mutually share risk and reward. The uncertainty of conventional insurance lays on lack of transparency as to what premium is for management expenses, how much portion is for claim payments, and what portion is for policyholders or shareholders a return.[19]

Moreover, many Muslim scholars consider the joint-stock insurance model speculative. In the joint-stock insurance model, participants seek to profit from the risk of an indeterminate event will occur.[20] This model comprises an undertaking by an insurer in exchange for consideration to make a payment to the insured if a specified event occurs. This commutative

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[17] *Uberrimae fidei* contracts or contracts of utmost good faith refer to a class of contracts where certain material facts to the contract are within the exclusive knowledge of one party and hence, the other party depends upon the good faith of the party with knowledge to disclose it. See Haemala Thanasegaran and Mohammed Shaiban, "Harmonisation of *Takaful* (Islamic Insurance) Regulation- a Realistic Goal or Improbable Ideal?," *Singapore Journal of Legal Studies* (2014).

[18] Ajmal Bhatty, *The Growing Importance of Takaful Insurance*, *Asia Regional Seminar* (Kuala Lumpur: 2017).

[19] Bhatty and Nisar, in *Takaful and Islamic Cooperative Finance: Challenges and Opportunities*.

[20] Serap Oguz Gonulal, ProQuest, and C. S. A. ProQuest, *Takaful and Mutual Insurance [E-Book] Alternative Approaches to Managing Risks* (Washington, D.C.: Washington, D.C. : World Bank, 2012).

contract of the mainstream conventional insurance is specifically objectionable by Sharia. This type of contract unduly limits uncertainty and ambiguity in human lives. Muslims can take steps to minimize the impact of events; however, they believe that what happens is predetermined by God's will. Furthermore, Muslim scholars consider conventional insurance is prohibited because the insurers pay for a loss of human life which is priceless, and they aim to generate profit for their stakeholders not whom there are insuring. This conceptual paradigm is the essential differences between mainstream conventional insurance and Islamic insurance.[21]

Nonetheless, Islamic insurance is not a health care sharing ministry as developed by many faith-based communities in the United States, such as Samaritan Healthcare ministry, Medi-share, Liberty HealthShare, etc. Islamic insurance operator is a for-profit company and regulated by the government as an insurance service. Meanwhile, these faith-based communities established health care sharing ministry as non-profit entities and with the purpose of promoting certain religious values.[22] The Affordable Care Act or Obamacare gives exemption to the members of health care sharing ministry plans due to this religious reason (which will end after 2018). They are exempt from the mandate to purchase insurance or face financial penalties.

These health-sharing plans necessitate the religious devotion of the members. The members need to obey specific behavior rules; for instance, they are not allowed to smoke, to use illegal drugs, to drink heavily, and to abuse prescription medications. These plans also are not covering medical expenses that are incurred from behavior that is deemed immoral, such as out-of-wedlock births or drunken-driving accidents, or medical procedures that conservative Christians oppose, such as abortion and gender-reassignment surgery, or even birth control, as required under Obamacare. The members must sign documents agreeing to obey those rules including going to church regularly and being faithful in their marriage. Their pastor had to affirm that they were active in their faith community. Liberty HealthShare, based in Canton, Ohio, for example, requires its members to follow God's commandments in their daily lives. The provider

[21] Hussein A Abdou, Ali Khurshid, and Roger J. Lister, "A Comparative Study of Takaful and Conventional Insurance: Empirical Evidence from the Malaysian Market," *Insurance Markets and Companies: Analyses and Actuarial Computations* 5, no. 1 (2014): 22–34.

[22] Serap Oguz Gonulal, *Takaful and Mutual Insurance [e-Book] Alternative Approaches to Managing Risks*, Directions in Development (Washington, D.C.). Finance (Washington, D.C.: World Bank, 2012).

is also constantly reminding them that the purpose of the plan is not to save money and gain profit but to honor the biblical teaching to “share one another’s burdens”.[23]

However, there is no unanimous agreement among all Muslims concerning the lawfulness of insurance transaction mentioned above. Muslim scholars from different legal schools of thought have different opinions on each detail of financial transactions, particularly on Islamic insurance. Some scholars even argue that conventional insurance is lawful under Sharia due to its benefits for individuals and society. Shaikh Abd al-Rahman Isa and Shaikh Muhammad al-Bahi, Professors of Al-Azhar University; Shaikh Muhammad Yusuf and Shaikh Abd al-Wahhab Khallaf from University of Cairo; Bahjah Hilmi, advisor of high court of Egypt; Muhammad Dasuki and Shaikh Muhammad Najatullah Shiddiqi from King Abdul Aziz University; Shaikh Muhammad Ahmad, economist of Pakistan; Shaikh Muhammad al-Madhani and Shaikh Mustafa Ahmad al–Zarqa from University of Syria, are example of Islamic scholars who do not prohibit conventional insurance services.[24] According to them, insurance is a cooperative; therefore, there is no usury applied in this type of transaction.

This disagreement is beyond the scope of this dissertation, although it may have some effects on the level of public acceptance toward insurance services. This dissertation focuses on Islamic insurance as a global social phenomenon, which was introduced, regulated and implemented widely by Muslim societies to replace conventional insurance.

Why is this important?

Islamic insurance’s geographical penetration is overgrowing. Islamic insurance is regionally significant in Gulf Cooperation Countries/GCC mainly in Saudi Arabia (KSA), Iran where the government prohibits conventional insurance and South and Southeast Asia with Malaysia at its core development. Islamic insurance’s growth has primarily outpaced the insurance sector growth in these regions. The demand has grown particularly within the GCC, as there is a shift

[23] Paul Demko and Renuka Rayasam, "Why Desperate Families Are Getting Religion on Health Coverage," *Politico*, last modified February 4, 2018.https://www.politico.com/magazine/story/2018/02/04/obamacare-religion-health-care-216933

[24] Syakir Sula, *Asuransi Syariah, Konsep dan Sistem Operasional*, page 71–76, as cited in Muhammad Maksum, "The Growth of Islamic Insurance in the World and Indonesia," *Al-Iqtishad* III, no. 1 (2011).

toward ethical, innovative and Sharia-compliant financial solutions. This growing need has also resulted in the launching of new Islamic insurance products, and these services are not only provided by Islamic countries, but also by American, European and Asian companies.[25] Islamic insurance is growing fast and reaching new places where conventional insurance has not been able to succeed, especially in life insurance.[26] In other words, the future development of global insurance cannot be separated from the development of Islamic insurance.

Despite its growing importance within the global financial system and in the daily lives of individuals, Islamic insurance is the least understood compared to the other Islamic Financial Instruments (IFIs). Islamic insurance's gross contribution (gross premiums) is estimated at around $14.9 billion in 2015.[27] After four decades, Islamic insurance's total contribution has grown from $750 million in the year 2000, to $2.5 billion (2006), and then $12.4 (up to 23.9 billion including Iran in 2012). With an annual growth rate of 20%, growth Islamic insurance contribution is expected to be around $52.5 billion in 2020. Islamic insurance has also brought many players in the business. It started by a handful of operators in 1980s, increased by 58 operators in 2003, and then 241 operators in 39 countries in 2012 with total global employees are estimated 70,010 (2013).[28] After 37 years (2016), there is a total of 308 Islamic insurance companies globally with mainly delivering insurance services in the Gulf Cooperation Council (GCC). Even American International Group, Inc., or AIG has also been offering Sharia-compliant home-owners insurance in the US through its subsidiary, Lexington Insurance Company. This company provides custom-tailored Sharia-compliant insurance solutions to consumers across the United States by working

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[25] Khalid Al-Amri, "Takaful Insurance Efficiency in the GCC Countries," *Humanomics* 31, no. 3 (2015), http://dx.doi.org/10.1108/H-05-2014-0039

[26] Bhatty.

[27] *Global Takaful Report 2017: Market Trends in Family and General Takaful*, last modified 10 July 2017 (Milliman, 2017), http://www.milliman.com/uploadedFiles/insight/2017/Takaful-2017-full-report.pdf. And also previous reports: World Insurance Factbook 2015"World Overview," III, , accessed January 22, 2017, http://www.iii.org/publications/international-insurance-fact-book-2016/world-overview, World Takaful Report 2016, accessed January 22, 2017, http://meglobaladvisors.com/insights/ , http://www.takaful.coop/images/stories/WTR%202008.pdf

[28] Hammad Bin Mohammed Smart University, *Takaful: Global Challenges to Growth, Performance, and Governance* (Dubai: Hammad Bin Mohammed Smart University, 2015), http://www.dcibf.ae/system/files/HBMSU_TakafulReport_NV%20Single%20Pages_LR.pdf

together with a New Jersey-based insurance brokerage firm, Zayan Takaful.[29] Despite this auspicious development, scholarly articles on the industry are sparse, particularly compared to the study on Islamic banking.

If the industry is less understood, it is more so than the politics involving the Islamic insurance industry. Although insurance, in general, is one of the largest state-regulated industries, scholarly literature on insurance has ignored the political economy aspects of insurance regulation. Most of the studies on insurance stress on the economic structure of the insurance industry and the economic theory of regulation. The economic theory of regulation contends that regulation is sought by the industry and designed for its own benefit. "The argument is because insurance issues are generally complex and rarely salient; the insurance industry should have a great advantage over consumer groups, bureaucrats, and political elites."[30] This theory sees insurance as a 'non-political' issue. Arguably, the same reason has made political scientists reluctant to discussing the Islamic insurance industry.

Furthermore, political scientists prefer to focus on social insurance, which is provided by the government rather than the one that is promoted by the private sector such as Islamic insurance. Governments spent much money through social insurance, which produced a substantial level of public expenditure in many developed economies. This scheme was the manifestation of what John G. Ruggie once called 'embedded liberalism': a global order made up of free-market societies with a compromise that allowed compensation for those who lost out from trade liberalization.[31] Protecting the population against economic insecurity is a way of ensuring the dynamism of the economy to be politically sustainable and morally defensible.

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[29] Insurance Journal, "Lawsuit Seeks to Stop U.S. Bailout of Aig as Anti-Christian, Anti-U.S," (2008), accessed 16 February 2017, http://www.insurancejournal.com/news/national/2008/12/16/96349.htm. More info on Zayan Takaful http://www.zayantakaful.com/about-us.php

[30] A salient issue is one characterized by intense conflict of a broad scope such as hazardous waste, mining industry, etc. A complex issue requires specialized knowledge and training to address the factual questions of regulations. Insurance regulation and banking are considered as complex regulatory area. See Kenneth J. Meier, *The Political Economy of Regulation the Case of Insurance* (Albany : State University of New York Press, 1988).

[31] In his essay published in 1982 by the Journal of International Organization, Ruggie describes how the global market system cannot last without social legitimacy. For that reason, the post-war global economy was created by including compensations for the ones who are harmed by the system. In many European countries, this compromise took the form of generous welfare states while in the United States it took a specific compensation program called Trade Adjustment Assistance (TAA). Unemployment insurance and job retraining are some of the instances of this program. John Gerard Ruggie, "International Regimes, Transactions, and Change: Embedded

However, the acceleration of automation and globalization limit the ability of the national government in protecting its domestic workers. There has been a transfer of risk from previously managed by the state or employer to the individual. Everyone must decide by him or herself how to handle his or her pension plan, investment, and saving.[32] As a result, insurance companies have become the dominant service provider for individuals and organizations to plan their future and protect them from losses. Rather than seeing this process as natural, we need to examine the homogenizing trend of the current neoliberalism. Perhaps, the growing importance of private-based Islamic insurance is as an instance of "The Retreat of the State" in the Islamdom.[33]

Furthermore, even though the development of Islamic insurance is a clear manifestation of Islamic revival,[34] political scientists have rarely put attention to this development compared to the issue of political Islam, radicalization, or even terrorism. It is surprising, especially when we understand that Islamic finance instruments including Islamic insurance are Muslims' responses to capitalism as a social and economic phenomenon.[35] One of prominent contemporary Islamic scholars in the West, Shaikh Hamza Yusuf, suggests that the single most important aspect of the Sharia after personal law of marriage are the commercial laws. Also, he adds that most Islamic books on Islamic law deal with issues on commerce.[36]

Liberalism in the Postwar Economic Order," *International Organization* 36, no. 2 (1982), http://dx.doi.org/10.1017/S0020818300018993.

[32] Jacob S. Hacker, *The Great Risk Shift: The New Economic Insecurity and the Decline of the American Dream* (New York: Oxford University Press, 2008).

[33] Susan Strange suggests a thesis of "the Retreat of the State" to show the dominance of the institution of market in our lives. She argued that the Market currently is the only remaining viable institution for people to take refuge from the current economic insecurity. Interestingly, she used the case study of global insurance as one of evidences to support her thesis. Moreover, she mentioned that the political economy study on insurance was very rare. see Susan Strange, *The Retreat of the State the Diffusion of Power in the World Economy* (New York : Cambridge University Press, 1996).

[34] Ermin Sinanović defined Islamic Revival as "a broad social phenomenon which includes all those social and political actors whose aim is to re-establish and re-institute Islamic teachings, in their broadest sense, into the societies in which they live." The main objective has been engaging modernity in ways congruent with Islamic tradition. Thus, Islamic Revival is not simply equivalent with popular religiosity; furthermore, it is a deep commitment of religiosity that is articulated to address problems or crisis. See Ermin Sinanović, "Islamic Revival as Development: Discourses on Islam, Modernity, and Democracy since the 1950s," *Politics, Religion & Ideology* 13, no. 1 (2012), http://dx.doi.org/10.1080/21567689.2012.659500.

[35] Charles Tripp, *Islam and the Moral Economy: The Challenge of Capitalism* (Cambridge: Cambridge University Press, 2006); Jonathan Ercanbrack, *The Transformation of Islamic Law in Global Financial Markets [E-Book]* (Cambridge, England : Cambridge University Press, 2015).

[36] Hamza Yusuf, interview by Scott MacLeod, October 5, 2015, The Cairo Review of Global Affairs, https://www.thecairoreview.com/q-a/all-american-sheikh/.

Islamic insurance shows how modern Muslims adapt their traditions to engage with today's world particularly the growing economic insecurity. It is an example of strategies that have enabled Muslims to remain true to their faith while engaging effectively with a world, not of their own making.[37] This dissertation wants to present the transformation of Muslim societies, particularly about the interaction between what Muslims believe (religion) and what, as a consequence, they do in politics and economics.

Furthermore, this research intends to give a scientific contribution toward the existing literature on Islamic insurance and International Political Economy (IPE) in several ways. Firstly, most research on Islamic insurance up to now has been survey driven and quantitative. This dissertation argues for qualitative research as a means of adding breadth and depth to existing studies of insurance implementation. Secondly, it intends to fill the gap within the studies of Islamic insurance development from its political determinants. The purpose is to understand how fate: potential harm, risk, crisis, economic insecurity, are manufactured and controlled in cultural and politico-economic context. Thirdly, it broadens the discussion of comparative IPE by including the social dimension of its analysis. It concerns how meaning ascribed to insurance changes over time, which is the behavior, the habit, and action of the consumers and providers within the system. The following paragraphs provide these expected contributions in further details.

Aside from rational calculation, historical circumstances are also essential to understand the context of an economic institution such as Islamic insurance. The defining characteristic of the historical view is its emphasis on `path dependence': ways in which the cumulative past, including the history of shocks and their effects, change the structure of the economy. Most studies on Islamic insurance have an underlining assumption that Islamic insurance will eventually be accepted by Muslim societies universally. As they become more modern and religious, they become more acceptable toward modern financial schemes such as Islamic banking and Islamic insurance.

On the contrary, the study of its historical context might push us to review this modernist view. A country with under-developed Islamic insurance may show a different path of response against economic insecurity. Probably, the private-sector-led Islamic insurance just does not fit

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[37] Tripp.

for that country. Some Muslim majority countries may pursue other ways of providing economic protection to their citizens such as through state or community-based assistance. The development gap in Islamic insurance and the various adjustments help us to identify different patterns of national response. This political process may depend not on the influence of doctrinal forms of Islam, but on historically, sociologically, and ideologically determined pattern of political agency.[38] In line with that, it may refute a simple notion of homogenization of global Islamic finance.

On the other hand, we cannot easily ignore the force of globalization of finance. It creates institutions and standards across different national boundaries. Thus, studying Islamic insurance can help us to examine the patterns of change within the Muslim societies especially in its relation to the economy. The consensus among historians suggests in the pre-modern Muslim societies economically defined social classes were relatively less significant as the famous Islamic historian, Ira Lapidus had claimed. [39]The remaining puzzle would be whether this claim is still valid within the current context of economic globalization.

In conclusion, this study is expected to broaden the theoretical discussion on comparative IPE. The works of such notables as Lindblom along with economists Robert Heilbroner and Lester Thurow argue that states and markets do not exist in a vacuum.[40] There are usually many different social groups within a state who share identities, norms, associations based on tribal ties, ethnicity, religion, or gender. Examining the societal aspect helps us to understand the context where political economy institutions exist. Studying a value-laden financial service such as Islamic insurance helps us understand the relationship between political economy and cultural differences. Economic activity is not merely a process of producing, accumulating and distributing wealth, but it is also a cultural process where people construct meaning. Therefore, removing

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[38] Clive S. Kessler, "Islam, Society and Political Behaviour: Some Comparative Implication of the Malay Case," *British Journal of Sociology* 23 (1979): 33–50.

[39] Lapidus., page 486.

[40] See Charles Lindblom, *The Market System: What It Is, How It Works, and What to Make of It* (New Haven, CT: Yale University Press, 2001), page 23. And, Robert Heilbroner and Lester Thurow, "Capitalism: Where Do We Come From?," in *Economics Explained: Everything You Need to Know About How the Economy Works and Where It's Going* (New York: Simon & Schuster, 1994).

cultural particularities in political economy analysis means dismissing context where our institutions exist.

Finally, yet importantly, studying the context of institutions has practical consequences. Unless we learn to link cultural, local, domestic to the economic, international, and global, we will not be able to identify predictions and policies that work better.

Case studies: three countries, three trajectories

This study investigates the causes of Islamic insurance development gap between three Muslim majority countries: Indonesia, Malaysia, and Pakistan. Malaysia has shown a significant growth rate in Islamic insurance demand and outpacing conventional insurance, while other countries including Indonesia and Pakistan, the home for 225 million and 200.3 million or 12.7% and 11% of the world's Muslims,[41] are still standing far behind Malaysia. Not only different in growth, but these three countries also seem to have different strategies in developing their Islamic insurance industries.

Since the 1980s, Indonesia, Malaysia, and Pakistan have experienced globalization in two folds: Islamization and economic liberalization. The 1979 revolution in Iran had an enormous global effect. It was for the first time Islamists gained power in a modern state. This event coincided with, and some have argued spurred, a broader resurgence of Islam around the world, including in these three countries.[42]

Abbot and Gregorios-Pippas define Islamization as 'the intensification of Islamic influence on social, cultural, economic and political relations.'[43] There was an increasing religious commitment toward Islam among the middle classes in these countries. For instance, many Muslim women started using the veil in public. In many urban areas, *Madrasahs* or Islamic schools were established. The number of Muslim middle classes were increasing; consequently, it also led to an increase in their political demand and economic influences. They demanded the expansion of Sharia law in the judicial system. Some scholars prefer to use the term 'Islamic

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[41] Central Intelligence Agency, *The World Factbook*.
[42] John L. Esposito, *Islam and Politics*, 4th ed. (Syracuse, N.Y. : Syracuse University Press, 1998), page 309-310.
[43] Jason P. Abbott and Sophie Gregorios-Pippas, "Islamization in Malaysia: Processes and Dynamics," *Contemporary Politics* 16, no. 2 (2010 2010), http://dx.doi.org/10.1080/13569771003783851.

revival' instead of Islamization to label specifically the phenomenon that happened in the post-1970s and to underline the growing universalistic Islamic identity, which transcends national and ethnic customs.[44] In this dissertation, both terms are used interchangeably.

At the same time, the economic stagflation of the 1970s encouraged many countries to look for a new economic system. Starting with Chile in 1975, various governments adopted and implemented liberal economic policies. Adding to that, the collapse of the Communist bloc at the end of the late 1980s generated political opposition to state interventionism in favor of unregulated market policies.

Beginning in the early 1980s, Indonesia embarked on the most comprehensive trade liberalization program in its history under President Soeharto. The long-term goal of the reform program was to replace Indonesia's industrial development strategy of import-substitution industrialization with one of export-oriented industrial growth. In Malaysia, Dr. Mahathir Mohamad was inaugurated as the Prime Minister of Malaysia in 1981 with main agendas to boost Malaysia's economy and to respond to the growing political threat from the Malaysian Islamist political party of PAS. Meanwhile, the government of Pakistan People's Party (PPP) was ousted in a coup d'état led by a former Army general, Zia-ul-Haq. He then became the sixth President of Pakistan with two cornerstones economic policy, including liberalization and Islamization of the economy. Islamic finance emerged within this context, in which the waves of Islamization and economic liberalization were sweeping the globe.

Indonesia, Malaysia, and Pakistan were the pioneers of Islamic finance, not only in the region but also in the world. Currently, these countries are the three most significant Islamic insurance markets in Asia. They are similar in many important dimensions. Islam has a prominent role in the social and political lives of the countries. Their population is majority Muslims. Pakistan declares itself as an Islamic state, while Malaysia gives special status for Islam as the religion of the Federation. Indonesia is not an Islamic state nor gives higher status to Islam, but Islam is the most adhered to religion in Indonesia, with around 87.2% of the population are Muslims. The

[44] see Sinanović; Lapidus, page 828; and Olivier Roy, *The Failure of Political Islam* (Cambridge, Mass. : Harvard University Press, 1994).

majority of Indonesian and Malaysian Muslims follow the Shafii School of law (*madhhab*).[45] Meanwhile, most Pakistanis are Hanafis with an also significant number of Shafii followers.[46] The government of Indonesia provides legal protection and financial support for not only Islam but also other five other religions. The Constitution of Indonesia also states that Indonesia is not a secular but a religious country.

The political economy situation of these three countries before the year of 2000 was also similar. They had authoritarian governments who controlled their social and cultural institutions. These countries had elements of democracy, such as general election and mass media, but the governments had enormous power and resources to ensure that these democratic elements did not work against them. There was widespread government favoritism in the distribution of fiscal expenditures and extensive political influence in the allocation of credit. On the other hand, the governments did not provide vast social security benefits for their general populations. These governments had been looking to several approaches of reducing the burden on their fiscal budgets arising from benefits being paid out to their growing population, particularly since the 1980s.

Moreover, there was no compulsory insurance introduced in these countries (except for Indonesia after 2014 with a universal healthcare system of JKN). The leaders had preference over liberal economic policies but wanted to maintain their political control at the same time. The ability to distribute economic resources among their supporters was the key to their political successes. Leaders in each country were avowed nationalists and maintained extensive personal control over the formation of economic policy.

Indonesia, Malaysia, and Pakistan are multi-ethnic and multi-religious countries. There are over 300 ethnic groups live in an archipelago of 17,508 islands of Indonesia with Javanese constitutes the largest group. There is also diversity in the religious affiliation among Indonesians. The government only recognizes six official religions, but there are more than 245 non-official

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[45] Pew Research Center's Forum on Religion & Public Life, *The Future of the Global Muslim Population: Projection for 2010-2030* (PewResearchCenter, 2011), https://www.pewforum.org/2011/01/27/future-of-the-global-muslim-population-about/.
[46] Ibid.

religions in Indonesia, according to the Indonesian Conference on Religion and Peace (ICRP).[47] Malaysia society consists of three major ethnic groups: Malays, Chinese-Malaysian, and Indian-Malaysia. In the eastern part of Malaysia, there is also a small number population of indigenous Bornean. Islam is the official religion, but Malaysia acknowledges the freedom of religion. As of the 2010 Population and Housing Census, 61.3 percent of the population practices Islam; 19.8 percent Buddhism; 9.2 percent Christianity; 6.3 percent Hinduism; and 3.4 percent traditional Chinese religions. The remainder is other faiths, including Animism, Folk religion, Sikhism, Baha'i Faith, and other belief systems.[48]

Meanwhile, Islam is the state religion of Pakistan, and around 98% of Pakistanis are Muslims. The majority are Sunni, and 6% of them are Shia.[49] Other data shows that Shia-Pakistani population reaches 10-15% of the total Muslim population of Pakistan.[50] Pakistan consists of diverse ethnic communities. The major ethnic groups in Pakistan in numerical size include Punjabis, Pashtuns, Sindhis, Siddis, Saraikis, Muhajirs, Baloch, Hindkowans, Chitralis, Gujarati and other smaller groups.[51]

Indonesia and Malaysia are two neighboring countries located in Southeast Asia region and share many similarities beyond the similarity in religion. These include standard frames of reference in history and culture. Furthermore, Indonesia and Malaysia are also working closely together regionally and internationally. They are the founding members of ASEAN and APEC, and members of the Non-aligned Movement and Organization of Islamic Cooperation (OIC).

Despite sharing so many similarities, they achieve different levels of Islamic insurance development and Islamic finance in general. Malaysia has become the hub of Islamic finance of Southeast Asia and the world, while Indonesia still has a vast untapped market. Not only in Islamic insurance but Indonesia life insurance penetration was also 0.99% in 2015, lower than

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[47] ICRP as cited in *Margareth S. Aritonang, "Government to Recognize Minority Faiths," the Jakarta Post, November 7, 2014.* http://www.thejakartapost.com/news/2014/11/07/government-recognize-minority-faiths.html
[48] Perangkaan Malaysia. Jabatan, *Taburan Penduduk Dan Ciri-Ciri Asas Demografi = : Population Distribution and Basic Demographic Characteristics* ([Kuala Lumpur]: Jabatan Perangkaan Malaysia, 2011), page 82. Retrieved 10 October 2018. https://copac.jisc.ac.uk/id/2721354?style=html
[49] Pew Research Center, *The World's Muslims: Unity and Diversity* (2012), accessed 16 October 2018, https://www.pewresearch.org/wp-content/uploads/sites/7/2012/08/the-worlds-muslims-full-report.pdf; ibid.
[50] Central Intelligence Agency, *South Asia: Pakistan*, *The World Factbook* (2010).
[51] Ibid.

neighboring Malaysia with 3.33%.[52] It is partly due to the differences in the compulsory insurance regulations. The mandatory portion of insurance in both countries are small. However, Malaysia has a higher requirement than Indonesia. For instance, Indonesia requires only a basic life and accident insurance for a driver of an automobile, which includes in the vehicle registration and driver license fee. Although the tariff is standardized, Malaysia requires third-party protection in vehicle insurance.

Furthermore, Malaysia has been officially developing Islamic finance since 1983 (Islamic insurance in 1984) with high government commitment and top-down approach comprehensively and pragmatically. On the other hand, the Government of Indonesia only started to support the development of Islamic finance in 1992 and Islamic insurance in 1994. There are less government support and more community initiative from below in Indonesia's Islamic finance development.

In 2016, total premiums and contributions of Malaysia's insurance sector increased by 4.4% to RM 61.3 billion or USD 14 billion (2015: +4% to RM 58.7 billion), while combined insurance and Islamic insurance assets expanded by 5% to RM 277 billion or USD 64 billion (2015: +5.7% to RM 263.8 billion). There were also 55 insurers and Islamic insurance operators, including reinsurers and Islamic re-insurance operators, in the industry as at end-2016.[53] Altogether, Malaysia has been contributing by 70% of the total regional market of Southeast Asia and 13% of the global market of Islamic insurance, respectively.

Meanwhile, Indonesia Islamic insurance sector has been showing significant growth too by having the contribution of 19% of the total regional market. In 2016, Islamic insurance in Indonesia accounted for 6.2 percent of the overall Indonesia insurance market with asset more than 42 trillion IDR (3.1 million USD).[54] Islamic insurance was introduced to Indonesian society through the establishment of PT Syarikat Takaful Indonesia (Takaful Indonesia) on 24 February

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[52] Verdict Staff, "Indonesia Hits the "Sweet Spot" for Life Insurance Growth," (2016), accessed 28 April 2019, https://www.verdict.co.uk/life-insurance-international/features/indonesia-hits-the-sweet-spot-for-life-insurance-growth-5036980/.

[53] Bank Negara Malaysia, *Financial Stability and Payment System Report 2016* (Bank Negara Malaysia, 2016), accessed 7 August 2017, http://www.bnm.gov.my/files/publication/fsps/en/2016/cp03.pdf.Accessed date: August 7, 2017.

[54] The Financial Service Authority of Indonesia (OJK), "Daftar Perusahaan Asuransi Umum Syariah (List of Sharia Insurance Companies)," (2015), accessed 28 April 2019, https://www.ojk.go.id/Files/statistik/26102015daftarperusahaanasuransisyariah.pdf.

1994. It was the first Sharia-compliant insurance company in Indonesia, which was endorsed by ICMI (Indonesian Association of Muslim Intellectuals) and promoted through Islamic informal and formal organizations. Since then, Indonesia's Islamic insurance has now developed into 20 Family Takaful companies, which consist of 3 Family Takaful companies and 17 units of Family Takaful, and 25 General Takaful composed of 2 fully-fledged Takaful companies and 23 units, and three Islamic re-insurance windows.[55] In 2015, the Islamic Insurance Association of Indonesia (AASI) had 61 Islamic insurance companies listed as its members.[56] The introduction of the new insurance law of 2014 was partly responsible for this positive development.

Moreover, *microtakaful* or micro-Islamic insurance has been utilized to help poor especially in rural Indonesia. Through this micro Islamic insurance program, poor people only need to buy monthly premium of 5,000 IDR (50 cents) to receive proper health care against dengue fever. Micro Islamic insurance in Indonesia is an instance of the bottom-up approach of Indonesia's Islamic finance strategy. It is based on Indonesia's communitarian tradition, which has provided a strong foundation for the national economy. On the other hand, micro-Islamic insurance is lacking in Malaysia. Malaysia's Islamic insurance companies focus more on the middle class and affluent Malay Muslims. Instead of providing social insurance, the state governments rely on the religious charity of zakat to assist their poor population.

In sum, Malaysia's Islamic insurance industry has higher growth compared to Indonesia. Moreover, there is not the only gap in the level of development, but also differences in strategies. These two neighboring nations have different priorities related to the development of their Islamic insurance structure.[57]

Pakistan shows another different story on its Islamic insurance development. In 2016, Pakistan was the third largest Takaful market in Asia along with Malaysia and Indonesia.[58]

[55] Islamic window refers to commercial bank or insurance company that offers Islamic insurance products. See Islamic Finance News, "What Does the Future Hold for the Takaful Industry in Indonesia," *IFN Roundtable* (2014), accessed 28 April 2018, http://islamicfinancenews.com/contents/roundtables/indonesia/Indonesia.pdf.
[56] Republika, "Aset Asuransi Syariah Capai 5,43 Persen (Islamic Insurance Asset Reaches 5.43 Percent)," (23 March 2016), accessed 28 May 2018, https://www.republika.co.id/berita/koran/syariah-koran/16/03/23/o4hcs95-aset-asuransi-syariah-capai-543-persen.
[57] Milliman, *Global Takaful Report 2017: Market Trends in Family and General Takaful* (2017), accessed 8 August 2017, http://www.milliman.com/uploadedFiles/insight/2017/Takaful-2017-full-report.pdf; ibid.
[58] Middle East Global Advisor & Finance Forward, *World Takaful Report 2016: Connecting the Dots, Forging the Future* (2016), accessed 9 August 2017, http://www.takafulprimer.com/main/downloads/ms_5860.pdf.

Pakistan is an Islamic state. The creation of Pakistan was to establish land for Muslims. Demographically, Pakistan is more like Indonesia. Almost 95% of 180 million Pakistanis are Muslim.

The government of Pakistan has been very involved in promoting various programs to bring Pakistan law in line with the principle of Sharia law. For instance, approximately 7,000 interest-free counters were opened at all the nationalized commercial banks in January 1980, making Pakistan the first country in the Muslim world with the largest number of Islamic banking. In 2012, the Securities and Exchange Commission of Pakistan, through notification S.R.O 877(I)/2012 dated July 16, 2012, issued the Takaful rules 2012, allowing conventional insurers to operate Islamic insurance windows alongside their existing conventional insurance business, and conduct Islamic insurance business.

Nevertheless, Pakistan has a very small Islamic insurance market (both total Islamic insurance penetration and density) compared to Malaysia, and even to Indonesia. There was no Islamic insurance company in Pakistan before 2006, and then only five companies operated in 2012. In 2010, the gross premium of Islamic insurance in Pakistan was just US$ 25.92 million, which is quite small compared to Malaysia with US$ 1.5 billion within the same year.[59] Pakistan started the Islamization of its economy since the 1980s, but it is not clear why Pakistan delayed the development of Islamic insurance until 2012. Pakistan preferred to focus on the implementation of Zakat (poor-due) to provide economic assistance for most of its poor population.

Indeed, there are some differences in their economic characteristics, such as the level of poverty and globalization that influence the growth and the direction of countries' Islamic insurance development. Pakistan has a higher level of poverty and a lesser connection to the global economy compares to Indonesia and Malaysia. However, this economic factor alone does not drive outcomes. Moreover, if this is more about religion as many insurance scholars suggested, what influence the acceptance toward Islamic insurance among the three countries' population who profess the same religion of Islam? The variation between countries is still

[59] Abdul Rahim Abdul Wahab, "Takaful Developments in Pakistan & Challenges Globally" (paper presented at the Amana Takaful Conference, Sri Lanka, 22 November 2011).

puzzling. Consideration of the political and social aspects of Islamic insurance development in these countries is needed to complete the story. This dissertation project investigates various socio-political factors contributing to this gap and their different trajectories.

'Political life' and 'social life' of Islamic insurance

My theory on the development of Islamic insurance rests on the analysis of Islamic insurance as a product of political decision and social practice. It focuses on how the decision of political actors to embrace and regulate Islamic insurance as a state's policy and the acceptance of public of Islamic insurance in their daily lives influence the development gap of Islamic insurance between the three countries. This dissertation aims to understand the whole picture of Islamic insurance development; therefore, it concerns less on how an increase or decrease in a unit of independent variables influences changes in the unit of dependent variables.

The literature on Islamic insurance suggests most demographic and economic factors for conventional insurance demand are also responsible for the development of Islamic insurance in the countries. Although Islamic insurance was designed as an alternative to conventional insurance, it needs similar conditions to grow. The factors such as inflation, income, education, urbanization, and dependency ratio are affecting the country's Islamic insurance development. These factors are essential; however, they cannot fully explain the reason why the government and its people supporting or rejecting Islamic insurance as an accepted and normative practice within society. Those findings are beneficial only when we disregard the historical context and socio-political particularities of the countries. For instance, the increase in income does not necessarily affect Islamic insurance development if the government outlaws its practice in the first place.

Moreover, those variables also cannot depict the reasons why Islamic insurance is organized and structured in a certain way; for instance, the way dispute should be solved. The law in Malaysia gives that authority to civilian court, while in Indonesia dispute settlement is managed under Islamic court jurisdiction. So, why they introduce it in the first place? Why the government regulates it? These are political and cultural related questions, which cannot be answered without understanding the historical context of Islamic insurance in the country.

As mentioned before, most research on insurance to date has been survey-driven and quantitative. This dissertation makes a case for qualitative research on the 'political life' and the 'social life' of Islamic insurance in Indonesia, Malaysia, and Pakistan as a means of adding breadth and depth to existing studies of insurance implementation.

The term 'political life of Islamic insurance' is developed based on the argument that Islamic insurance arrangements are not a passive response to some efficiency criterion but rather the product of political deals within country's polity that determine which laws are passed.[60] The payment, involving all the details of how providers are paid, incentives, and so on; and organization, the structure of Islamic insurance system, risk pooling and the division of labor of institutions within it are an outcome of political decisions. The political life of Islamic insurance in these three countries is examined through the analysis of political coalitions behind the institutionalization of Islamic insurance and Islamic finance in general since the 1980s.

The usage of the term 'social life of Islamic insurance' refers to a framework for understanding Islamic insurance as a commodity whose worth lies both within and beyond its exchange value.[61] It calls attention to how insurance moves between registers of value among different stakeholders and at various scales of analysis. It also encompasses how meaning ascribed to insurance changes over time. It is the behavior, the habit, and action of the consumers and providers within the system. Based on Ami Dao's ideas on the social life of health insurance, we can analyze the social life of Islamic insurance through the interaction of various factors, including the sociocultural, economic, political, historical, and "global-local" that contribute to the "careers" of Islamic insurance plans in these countries.[62]

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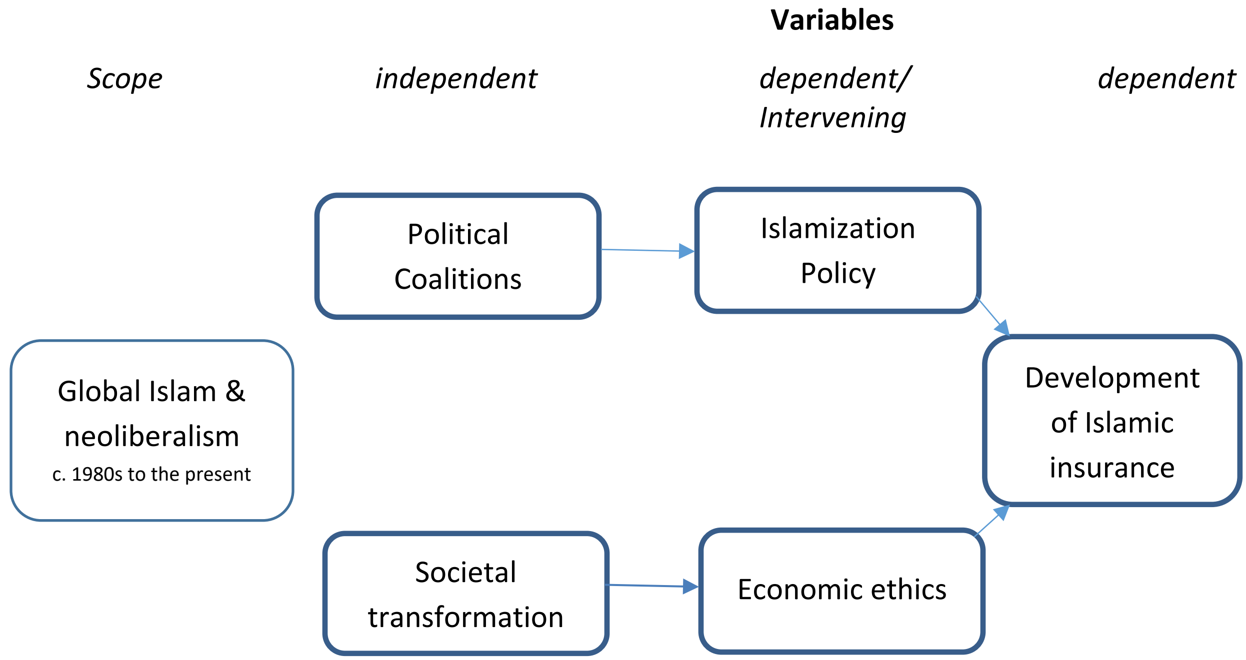
[60]Charles W Calomiris, *Fragile by Design the Political Origins of Banking Crises and Scarce Credit* (Princeton Economic History of the Western World, 2014).

[61] Arjun Appadurai, *The Social Life of Things: Commodities in Cultural Perspective* (Cambridge: Cambridge University Press, 1986).

[62] Amy Dao, "The Social Life of Health Insurance in Low-to Middle-Income Countries: An Anthropological Research Agenda," *Medical Anthropology Quarterly* 30, no. 1 (2015).

Figure 1-1: Theoretical Framework



The diagram above summarizes the arguments of political life and social life of Islamic insurance. Chapter II, literature review, presents the reasoning behind this theoretical framework in further detail. However, the purpose of this dissertation is not to test hypotheses nor to make a generalization. The theoretical framework shown above is a descriptive tool and it should not be treated as a universal model. This dissertation is case studies that observe, explore the cause and effect relationships between variables over time and across scales, and trace processes of Islamic insurance development of these countries. The intention is to trace the political coalition processes behind the development of Islamic insurance, examine the influence of political and economic actors and institutions, look at the effect of 'path dependence' on each country, and to show in detail the ebb and flow of religious devotion, ideologies and self-definition of Muslims interacting with modernity and capitalism.

Data and methods

This dissertation draws on secondary works in several other disciplines: not just political science and history, but also anthropology, economics, sociology and religious studies. The design of this study mostly follows a qualitative research methodology specifically case study and combines a range of primarily qualitative approaches. It analyzes political parties and coalition platforms, organizations' charters, and press releases to trace contemporary and prior political norms, priorities, and strategies. Ethnographic and historical studies, documents, and secondary sources help to understand the social and cultural circumstances. Quantitative resources such as survey data and statistics are used when possible.

This dissertation focuses on the period between the initiations of Islamic insurance regulation in each country until the present time. However, the major part of this research will be dedicated to examining the socio-political process surrounding the enactment of those regulations. The different starting date of Islamic insurance development is in itself a puzzle as Indonesia, Malaysia, and Pakistan started the whole project of Islamization of economy relatively at the same time in the early 1980s. Therefore, the development of Islamic insurance cannot be separated from the development of other Islamic financial institutions such as Islamic bank and the implementation of religious tax of *Zakat*, and the role of Islam in these countries in general. Moreover, it is necessary to discuss the historical background as far as since these countries became independent nations.

Data on national Islamic insurance growth of each country are available from many sources. However, Malaysia has an abundance of quantitative data on Islamic insurance; meanwhile, reliable quantitative data from Indonesia and Pakistan are scarce. In Malaysia, Bank Negara Malaysia provides both data on conventional insurance and Islamic insurance along with other economic indicators. The Central Bank of Indonesia does not regulate Islamic insurance and other insurance products. Indonesia Financial Services Authority (OJK) is the one who regulates, monitors, and provides up to date data on insurance including Islamic insurance. Data on Islamic insurance in Pakistan is still limited. The State Bank and Securities and Exchange Commission of Pakistan offer insurance data in one package; therefore, data on insurance premium from Islamic insurance companies and other private agencies are more reliable to be

used. Auditing and consulting firms provide annual growth data, market research and normative-juridical reports on insurance and Islamic insurance of many countries.

The primary goal of this research is to understand the Islamic insurance phenomenon by focusing on the total picture rather than breaking it down into variables. It is to see a holistic picture and depth of understanding of Islamic insurance development.[63] Therefore, this dissertation uses a method suggested by Calomiris and Faber in their study of the political origins of Banking Crises.

Different from other economists, Calomiris and Faber write 'narrative history' of six case studies to draw some general lessons on the banking system. They argue that considering the historical context to understand the factors that shape complex systems such as the banking system are important. Without that, we omitted the most important dimension that is time, which can lead to misinterpretation of the deeper meaning of the correlations between variables. They said:

> Researchers who do not take history seriously wind up reducing the study of complex banking systems to an analysis of correlations among various influences… This approach often fails to find the connections because the influences being modeled are considered without taking context into account. And when such a modeling approach does find empirical correlations, the meaning can be misinterpreted because the correlations identified by the researcher reflect deeper, omitted influences on all the variables being measured. [64]

Similarly, with its emphasis on the context-bound and holistic approach of theory generation, this dissertation seeks to understand Islamic insurance development by identifying and categorizing vital elements of the phenomenon that emerge from data, rather than to verify theory or to describe data. This method helps us to understand the complexity of the problem of Islamic insurance development in these three countries.

Lastly, Islamic insurance is part of a bigger Islamic finance regulatory structure. Some countries regulate it separately and in a very detail manner. Malaysia, for instance, has a very

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[63] Bruce L. Berg, *Qualitative Research Methods for the Social Sciences*, 4th ed. (Boston : Allyn and Bacon, 2001); John W. Creswell and Dana L. Miller, "Determining Validity in Qualitative Inquiry," *Theory Into Practice* 39, no. 3 (2000), http://dx.doi.org/10.1207/s15430421tip3903_2.
[64] Charles W. Calomiris, *Fragile by Design*, page 486.

sophisticated Islamic insurance program. In this case, we can expect more information and specific data on the political processes of Islamic insurance. Meanwhile, other countries regulate it together with other Islamic finance instruments. Therefore, there are not many specific data available except the data within the general discussion of the political processes of Islamic finance.

Dissertation organization

The dissertation consists of six chapters. As shown above, the Introduction Chapter provides an argument for the significance of the problem, contextualizes the study, and introduces the fundamental component of this dissertation. Islamic insurance has been rapidly growing in the Islamdom since the 1980s. However, there has been a development gap between countries. This dissertation is an effort to explain that gap in selected countries.

Chapter 2 is a literature review of this study. This chapter places the dissertation in the context of the previous research and scholarly material on Islamic insurance, insurance in general and International Political Economy (IPE). It addresses a gap in the literature on the lack of study on the political and social determinants of Islamic insurance development. This chapter provides a strong theoretical basis for the dissertation for analyzing the 'political life' and the 'social life' of Islamic insurance within Muslim societies.

The next three chapters are the empirical chapters of this dissertation. These chapters organize and report the study's main findings, identifying what is significant, and making sense of large amounts of data concerning the Islamic insurance development of the three countries. These chapters are organized similarly, and each country is fully discussed in one complete chapter. All chapters start with a brief introduction of the country, particularly the role of Islam in the country's political economy ecosystem. Then the chapters continue by elaboration of data, including quantitative and qualitative (narrative data), on the development of Islamic insurance in each country. The discussion on coalitional politics and social aspects of Islamic insurance are provided afterwards. These chapters synthesize and discuss the results considering the study's research questions, literature review, and conceptual framework. The three empirical chapters start with Chapter 3 on Malaysia, then Chapter 4 on Indonesia, and ends with Chapter 5 on

Pakistan. These chapters are the foundation for the reflections, conclusions, and recommendations that will appear in the next chapter.

The last chapter, Chapter 6, provides the conclusion of this research project and recommendation for further research. Moreover, this chapter offers a thorough reflection on the study's findings, and the practical and theoretical implication thereof. The goal is to discover what meaning we can make of them by comparing the findings both within and across country case studies, and with those of other studies. This chapter ends with the identification of relevant future research areas in the disciplines.

CHAPTER II

LITERATURE REVIEW

This literature review chapter discusses the factors of Islamic insurance development provided by the current research on Islamic insurance. It is also a detail elaboration of the theoretical framework presented previously in the introduction chapter. In general, the literature show most demographic and economic factors for conventional insurance demand are also responsible for the development of Islamic insurance in the countries. Although Islamic insurance was designed as an alternative to conventional insurance, it needs similar conditions to grow. The factors such as inflation, income, education, urbanization, and dependency ratio are affecting the country's Islamic insurance development. These factors are essential; however, they cannot fully explain for variations among the three countries of our case studies: Indonesia, Malaysia, and Pakistan. Therefore, it is essential to understand the correlations between those factors by considering the political and social institutions within which Islamic insurance systems are constructed.

This chapter starts by providing a general overview of the importance of insurance in international political economy (IPE) discourse. Then, it continues by reviewing the common explanations offered by conventional economists on Islamic insurance development. Almost all studies provide a static comparison by presenting Islamic insurance as a universal product that necessitates similar determinants to grow, regardless of countries' particularities. Next, this literature review elaborates alternative explanations consisting of two categories: political and social explanations. Lastly, this chapter provides a comprehensive synthesis of the literature review, arguing the importance of socio-political factors to understand Islamic insurance development in these three countries.

Insurance: an institutional history

Insurance is an institution created by humanity to handle the risk of economic loss. It provides constraints that structure how we manage economic risk.[65] The practice dates back to the Hammurabi Code, which offered basic insurance in that a debtor did not have to pay back his loans if some personal catastrophe made it impossible (disability, death, flooding, etc.).[66] Then, it developed into a sophisticated actuarial science when in 1654, Blaise Pascal and Pierre de Fermat discovered a way to understand the level of risk, thereby, actuaries can calculate the insurance rates. Using the probabilistic method, they counted the amount of capital needed to overcome future losses. Since then, insurance shifted the focus from preventing to compensating possible losses. This innovation makes insurance as an important part of the development of the market economy. It has enabled capital accumulation, especially for risky business ventures.[67]

In general, contemporary insurance can be categorized into two mechanisms: spreading risk among large numbers of people and/or moving risk to entities that can handle it. The collective insurance fund of the guild system during the Middle Ages was an example of spreading risk among group members (cooperative), while the practice of underwriting during voyages to the New World was an example of moving risk- the origin of joint-stock enterprises. Both are the core practices of contemporary insurance.[68]

Every civilization has been dealing with economic insecurity for so long. However, the concept of risk is quite modern. Risk is a concept to transform the unpredictable into something that calculable. The traditional society emphasizes on anticipation of the actual prevalence of life-threatening dangers, which lead to economic insecurity. God or Nature is the source of this unpredictable insecurity. Anthony Giddens argues that there has been a substantial historical

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[65] Douglass C. North defines institution as s are the humanly devised constraints that structure political, economic and social interaction. They consist of both informal constraints (sanctions, taboos, customs, traditions, and codes of conduct), and formal rules (constitutions, laws, property rights). See Douglass C. North*, "Institutions," Journal of Economic Perspectives 5, no. 1 Winter (1991).*

[66] *Investopedia*, s.v. "The History of Insurance," accessed 17 February 2017, http://www.investopedia.com/articles/08/history-of-insurance.asp.

[67] Moshe A. Milevsky, *Your Money Milestone: A Guide to Making the 9 Most Important Financial Decision of Your Life* (FT Press, 2010).

[68] Andrew Beattie, "The History of Insurance," (April 24 2007), accessed 17 February 2017, http://www.investopedia.com/articles/08/history-of-insurance.asp.

transformation of the nature of risk -and security.[69] People in the modern age are relatively more secure than they were in previous ages. They have longer life expectation and freedom from serious disease.

Nonetheless, the physical security of modern people is balanced by new risks: war, nuclear threat, motor accident, environmental degradation, etc. These risks are not generated by natural causes, but as results of modern social organization or so-called abstract system.[70] Furthermore, these new risks affect everyone or at least very large numbers of people on the planet.[71] The new risks are considered as manufactured risks, which resulted from the human activity. Therefore, instead of merely anticipation from the impact of natural causes as happened during the traditional society, control of risk is the essential feature of responding toward manufactured risks of modern society.

Modern Insurance is a modus operandi for modern society to control economic risk. It has been developed through the role of the state and the market, which are the two most important parts of four dimension of modernity discussed by Giddens.[72] State and market

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[69] Ulrich Beck also discuss the new nature of risk of modern society in his 1992 book on risk society. He argues that the modern society is facing different type of risk. It is a problem environmental hazard which cut across traditional inequalities of wealth and income. Furthermore, modernization dissolves traditional parameter of industrial society: class culture and consciousness, gender and family roles. See Ulrich Beck, *Risk Society: Towards a New Modernity* (London: Sage, 1992).

[70] Giddens defines abstract system as knowledge-based patterns of social behavior, coordinated through markets as well as bureaucracies, which govern the conditions of individual existence. The spread of these systems is global: 'In high modernity, the influence of distant happenings on proximate events, and on the intimacies of the self, becomes more and more commonplace. Anthony Giddens, *The Consequence of Modernity* (Stanford, California: Standford University Press, 1990).

[71] Ibid.

[72] Those four dimensions of modernity are world capitalist economy, nation-state system, world military order, and industrial development. World capitalist economy refers to states in which capitalist economic enterprise is the chief form of production. The domestic and international economic policies of these states involve many forms of regulation of economic activity. The second dimension of the nation state system refers to the replacement of “frontiers” by “borders” that brought the idea of Sovereignty: autonomy inside the territory claimed by the state is sanctioned by the recognition of borders by other states. Rather than creating class of authority, the institutional organization maintains an “insulation” of the economic from the political. This allows wide scope for the global activities of business corporations, which always have a home base within a particular state but may develop many other regional involvements elsewhere. Giddens argues that if nation-states are the principal “actors” within the global political order, corporations are the dominant agents within the world economy. See Anthony Giddens, *Modernity and Self-Identity Self and Society in the Late Modern Age* (Stanford, California: Stanford University Press, 1991), page 70-74.

become crucial actors because the traditional institutions and culture can no longer provide the necessary protection for modern people. Giddens argues:

> The security 'threat' which individuals face is, at base, the threat to their very identity from the ways in which abstract systems instead of Nature operate. The challenge to individuals is to construct and reconstruct their own identity, which is no longer given for them by traditional institutions and cultures but are constantly at risk. [73]

Adding to that, the informal mechanisms have become obsolete also because of the 'actuarial technique' itself. There is no need for 'community' or 'social capital' for modern insurance to work. In his work of *The Emergence of Risk Society: Insurance, Law, and the State*, Jonathan Simon asserts that the modern way of managing risk reconstructs individual and social phenomena as risk object rather than a moral agent and member of society. It focuses on one's risk profile rather than biographical individuals. Individual identity is a combination of variables associated with different categories and level of risk.

Furthermore, insurance provides a sense of security not by disciplining individuals and prevent harm through moral tools (e.g. rituals, punishment, and excommunication) but by calculating the aggregate cost in order to compensate for the harm. Using the example of auto insurance, Simon argues that the actuarial technique creates a new social fact. A traffic accident is no longer considered as a deviance act to be eliminated but as just a part of the consequences of living in society and has a significant probability of happening.[74] Statistics has replaced taboos and traditions in structuring the way we deal with economic risk.

Insurance managers offer us comfort for this economic insecurity through a promise to pay compensation for the losses. They convert our liability to risk into a liability to themselves to pay the cost of compensating us. Later on, this type of personal risk is multiplied by the increase in economic transactions. In a planned economy such as the former Soviet Union, State was the universal insurer. The government decided whose risks should be translated into costs, and it was the state that decided who should bear the cost. Mostly, the cost was imposed on the citizens

[73] Giddens, *The Consequence of Modernity*.

[74] Jonathan Simon, "The Emergence of a Risk Society-Insurance, Law, and the State," *Socialist Review*, no. 95 (1987).

in forms of taxes, inflation, in shortages, and poor public services. Usually, some resource transfers as in progressive taxation are used in this state-scheme mechanism.

On the contrary, the power to decide about risks is more mixed in the market economy. The main responsibility for insuring against risks of economic insecurity is left by the State to the individual that empower players in the market to decide. This means the individuals as potential buyer of insurance service and the seller are free to negotiate and take the decision on access, price, and availability of benefits. For that reason, Susan Strange argues insurance practices entail power relations. It lies on who is translating risks into a cost.[75]

Moreover, insurance as a global practice was indispensable for the development of the market economy. Strange considers insurance business as an instance of diffusion of power in the world economy. It is one of Strange's empirical proof of diffusion of power in the world economy: "that power has shifted "sideways" from states to market and other non-state actors who derive power from their market shares." The power relations are also reflected in whose favor it operates. As in the case insurance within the market economy, Strange states:

> When the insurance business is left to the market, the result is usually the rich, individually or collectively, can choose whether to translate, through insurance premiums, some element of risk into a cost. Insurance gives them the option. The poor, unable or unwilling, or both to pay the premiums are left with the risk.[76]

Competition does not necessarily eliminate the opportunity of monopoly by big companies. As the service becomes more global, the big global companies have a comparative advantage, especially compares to the developing countries, which act as state insurer. Therefore, developing countries tend to be more protective in term of their insurance businesses. Allowing saving to be converted into foreign currency -in the form of insurance premiums- out of national currency is considered as a threat to the well-being of their economy. According to Strange, therefore Brazil and India, among others, opposed the American proposal of extending

[75] Susan Strange, *The Retreat of the State* (New York: Cambridge University Press, 1996), page 49.
[76] Ibid.

the liberalization of goods into services including insurance in the mid-1980s during the GATT's Uruguay round.[77]

Many scholars argue that the institutionalization processes are in the direction toward a more economically efficient, complex, global and impersonal institution or market. It seems there is no place for the informal institution of insurance within the modern and globalized economy. It is far from it. Rather than disappearing, the personal and social alternatives of insurance are gaining importance in many places.[78] People turn again to the informal when 'the state is retreating' and at the same time, the market is operating against their favor. As some researchers have documented, poor farm-households are less keen to adopt high risk/high return technologies than rich households are. The consequence, there has been a very low insurance penetration among the poor. However, introducing formal insurance to the poor is not an easy task. It often generates a moral hazard among this community.[79]

Regarding Islamic insurance, Atiquzzafar Khan argues the Muslims first became aware of the practice of insurance because of trade contacts between Europe and the Ottoman Empire.[80] However, the Muslims did not develop insurance until the 21st century. In addition, in 1914, there were around 170 insurance companies offering insurance services: life, transport, and life insurance, in Istanbul, the capital of the Ottoman Empire. All of them were European companies with roughly one-thirds of these were German-speaking companies.[81]The possible reason is that cooperative practices in both personal and business life substantially reduce the need for insurance – a society is expected to take care of those in need. Insurance was not needed in the original Islamic Empire, despite the existence of an extensive global trade network.[82]

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[77] *Ibid,* page 130.

[78] Y Sawada, "Disasters, Household Decisions, and Insurance Mechanisms: A Review of Evidence and a Case Study from a Developing Country in Asia," *Asian Economic Policy Review* 12 (2017).

[79] Matthieu Delpierre, Bertrand Verheyden, and Stéphanie Weynants, "Is Informal Risk-Sharing Less Effective for the Poor? Risk Externalities and Moral Hazard in Mutual Insurance," *Journal of Development Economics* 118 (2016).

[80] Atiquzzafar Khan, "Insurance Aur Ijtima'i Fiqhi Idaron Ki Ara' [Insurance and the Opinions of Collective Institutions of Fiqh]" (paper presented at the Seminar on Collective Ijtihad, Evolutionary Change and Practical Methods, IRI, Islamabad2005).

[81] Swiss Re, "Insurance in the Ottoman Empire," (accessed 10 January 2018, http://history.swissre.com/item_detail.php?id=102&comefrom=item*60.

[82] Asad Zaman, "Islamic Economics: A Survey of the Literature," *Islamic Studies* 49, no. 1 (2010): 37–63, https://doi.org/10.2139/ssrn.1282786.

Furthermore, the central question related to insurance within Muslim societies is always about its permissibility. When questioned about the permissibility of insurance, scholars of Islamic law have generally given negative answers. While they recognized the utility of the practice, they found that it conflicts with Islamic law on several grounds of the uncertainty about the product received, the element of usury, and gambling as discussed before in the introduction of this dissertation.

Given the nearly unanimous verdict on the prohibition of insurance, the next question is what alternatives might be possible. Many of the Islamic scholars reject the approach of modifying existing institutions to conform to Islamic law and suggests that Muslims should develop Islamic alternatives to clarify the radical differences between Islamic and capitalist forms of insurance. They call this alternative insurance with unique name, Takaful. The scholars examine the purpose of various types of insurance contract, assesses the conformity between their purpose and Islamic law and historical precedence in the Islamic tradition, and suggests different methods to achieve the same purpose that are within the domain of Islamic law.[83]

Takaful or Islamic insurance has been promoted as an Islamic alternative for the immorality of conventional insurance. According to its supporters, Islamic insurance is not simply a compromised form of Western risk management. It is argued that the motivation of Islamic insurance is different from how the Victorian recasting of Christian duty to provide the family's future. Islamic insurance is claimed to be a tool not only for the benefit of individual and family, but also to reduce unequal wealth distribution in the society, which resulted from the interest-based economy.[84]

According to the Sharia, government-sponsored plans are generally acceptable. The reason is because Sharia provides ruling that governments are responsible for taking care of their citizens. Meanwhile, private sector insurance schemes are acceptable but with some conditions. The general principles on which private scheme of Islamic insurance are based are different from conventional insurance contracts. According to the Sharia, the foundation of assurance can be

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[83] Mahmood Ahmad Ghazi, *Report on Islamic Insurance System* (Islamabad: Government of Pakistan, Council of Islamic Ideology, 1992). As quoted by Zaman.

[84] Adam Burgess, "Socio-Historical Life Insurance Research, 'Moral' Obstacles and Sociology" (paper presented at the the 'Fate and Fortune' Series, Davis Center, Princeton2018), https://www.academia.edu/37026094/Socio-Historical_Life_Insurance_Research_Moral_Obstacles_and_Sociology.

based only on cooperation, mutual sympathy, brotherhood, and mutual guarantee. The system, which the real and basic aim is business, profit-making, and money is hoarding cannot be adopted. Islamic law permits only mutual insurance, where a group collectively safeguards the interests of its members and acts to support them in the case of damage.[85]

What we know about its determinants

Like conventional insurance, the country's Islamic insurance development is commonly measured by insurance penetration and density. Insurance penetration is expressed as a ratio of premium to another financial measure like Gross Domestic Product (GDP), while Insurance density refers to a product's number of customers by geographic area (country, state etc.). It is usually expressed a ratio of premium to a population. Both indicators comprise the insurance demand of the country.

In the literature of economics and finances, determinants of insurance demand in national level are divided into two broad categories of macroeconomic and demographic factors. A comprehensive study by Feyen, Lester, Rocha[86] concludes that life and non-life insurance sectors premiums 'are driven by per capita income, population size and density, demographic structures, income distribution, the size of the public pension system, state ownership of insurance companies, the availability of private credit, and religion'. Income is considered as the best predictor of insurance demand as it leads to more affordability and ultimate higher demand for an insurance product. Other studies regarding the demand for life insurance in the Muslim majority countries are also confirming this conclusion. Baharul-Ulum and Yaakob found that the GDP of the country plays a vital role in reshaping insurance demand in Malaysia.[87] In addition,

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[85] Zaman.

[86] Erik Lester Rodney Rocha Roberto Feyen, *What Drives the Development of the Insurance Sector? An Empirical Analysis Based on a Panel of Developed and Developing Countries*, *Policy Research Working Papers* (The World Bank, 2011).

[87]A.Z. K. Baharul-Ulum and R Yaakob, *Life Insurance's Demand: Role Played by Economic Variables–a Malaysian Case*, vol. 16, *the International Conference: Asia Pacific Business Environment: Innovative Responses to Regional Events* (Selangor: Shariah Journal, 2003).

Zerriaa and Noubbigh findings show the positive impact of GDP per capita income toward insurance demand across the MENA region.[88]

Demographic factors also play an important role. Expansion of cities and towns due to industrialization and urbanization provides opportunities for the insurance sector to grow especially in developing economies. Hwang and Gao found a positive impact of urbanization on saving propensity of urban people in China. They argue that insurance can play a vital role in providing protection and financial security to small families living in China's new urban centers. Not only China, life insurance products and urbanization are found positively related in other Asian countries too.[89] However, some studies have found an insignificant impact of urbanization on life insurance in Central and East European countries.[90] However, there is contradictory findings related to non-life insurance demand. Park and Lemaire found positive relationship of urbanization to non-life insurance demand while Treerattanapun found it insignificant.[91]Also, Simona Laura Dragos's comparative research founds a positive and significant impact on non-life insurance for both Asian and Central and East European countries (CEE). However, regarding life insurance, Dragos founds urbanization only has positive and significant impact in Asian region only.[92]

Financial sector development plays a vital role in economic growth through strengthening the financial institutions and building investors' confidence. Cash flows and financial assets securitization create a close link between financial sector developments and insurance demand.

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[88]Mouna Zerriaa and Hedi Noubbigh, "Determinants of Life Insurance Demand in the Mena Region," *Geneva Papers on Risk & Insurance* 41, no. 3 (2016), http://dx.doi.org/10.1057/gpp.2016.1.

[89] Tienyu Hwang and Simon Gao, "The Determinants of the Demand for Life Insurance in an Emerging Economy - the Case of China," *Managerial Finance* 29, no. 5/6 (2003), http://dx.doi.org/10.1108/03074350310768779.

[90] Thorsten Beck and Ian Webb, "Economic, Demographic, and Institutional Determinants of Life Insurance Consumption across Countries," *The World Bank Economic Review* 17, no. 1 (2003), http://dx.doi.org/10.1093/wber/lhg011.

[91] C. Park Sojung, Lemaire Jean, and Chua Choong Tze, "Is the Design of Bonus-Malus Systems Influenced by Insurance Maturity or National Culture? — Evidence from Asia," *The Geneva Papers on Risk and Insurance Issues and Practice* 35, no. S1 (2010), http://dx.doi.org/10.1057/gpp.2010.37. And Aranee Treerattanapun, "The Impact of Culture on Non-Life Insurance Consumption" (paper presented at the Wharton Research Scholars Project, Philadelphia, PA: The University of Pennsylvania2011).

[92] Simona Laura Dragos, "Life and Non-Life Insurance Demand: The Different Effects of Influence Factors in Emerging Countries from Europe and Asia," *Economic Research-Ekonomska Istraživanja* 27, no. 1 (2014), http://dx.doi.org/10.1080/1331677X.2014.952112.169–180.

On the other hand, after the global financial crisis, financial sectors (especially banking developments) more focused on insurance backed investments to minimize the unexpected losses. Financial sector development encourages investors to obtain ownership of financial assets to secure their future income and to expand their operations. Therefore, it generates the need to secure these assets through insurance products results in their increasing demand.[93]

Interestingly, Islam as religion is considered by many researchers as an obstacle to insurance development. According to their findings, most Muslim majority countries have a very low insurance demand. It is thought that the reason is that prohibition of usury and speculative economic activities. Researchers consider this prohibition makes Muslim population reluctance in buying conventional insurance premium. Presumably, this prohibition encourages the development of Takaful or Islamic insurance as alternative insurance.

Inflation is also an important factor, which has an ambiguous correlation with insurance development. Customers are sensitive to the change in inflation realized or anticipated, and this might result in reducing the consumption of insurance products.[94] It results in a decline of insurance demand. On the other hand, Hwang and Gao found that insurance demand, in the case of China, was not adversely affected by higher inflation. It is because the higher inflation period happens when there is also higher economic growth. In summary, people using these products were less responsive towards change in their demand for insurance products.[95]

Another significant demographic factor is education. Education is used as a proxy for the level of risk aversion and awareness. Most the studies indicate a positive relationship between general insurance and education illustrating that education enhances knowledge regarding financial stability threats, insurance benefits and awareness of risk mitigation.[96]

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[93] Donghui Li et al., "The Demand for Life Insurance in Oecd Countries," *Journal of Risk and Insurance* 74, no. 3 (2007), http://dx.doi.org/10.1111/j.1539-6975.2007.00228.x.637–652. http://dx.doi.org/10.1111/jori.2007.74.issue-3

[94] David F. Babbel, "Inflation, Indexation, and Life Insurance Sales in Brazil," *The Journal of Risk and Insurance* 48, no. 1 (1981), http://dx.doi.org/10.2307/252655. 111– 135. http://dx.doi.org/10.2307/252655 (Oxford: Hart Publishing, 2010), 120.

[95] Hwang and Gao.

[96] Mariya Neycheva, "The Role of Education for the Economic Growth of Bulgaria," *Economic, Management and Financial Markets* 9, no. 1 (2014).

Adding to education, the ratio of average family member's young and old dependent for support within the family is also an essential factor. It is defined as dependency ratio. Providing protection from financial hardships to their dependent family members is the basic driving force for the demand and consumption of these insurance products. Some studies have documented a positive relationship between dependency ratio and insurance demand.[97]

Several studies on Islamic insurance confirm similar findings. For example, a survey by Rahman, Rosylin, and Faizah[98] founds a positive relationship of GDP per capita and Islamic insurance demand in Malaysia. Both conventional insurance and Islamic insurance tend to develop well in the country with high GDP per capita. As the people are getting wealthier, they can spend some of their income for insurance, regardless the type of the insurance. Other economic aspect that relevant to Islamic insurance is inflation. Redzuan et al. depicted a negative but insignificant relationship of inflation with Family Takaful demand. They asserted that inflation depresses the value of financial assets, life insurance and Family Takaful products.[99]

Studies on factors of education have shown consistent relationship with conventional insurance, but it show mixed evidence in relation to Islamic insurance.[100] Hawariyuni in her study indicated that education is not a significant variable affecting Islamic insurance demand, as it is not necessary that highly educated people buy these Islamic insurance products. [101] Sherif determined that education was found having a positive influence on Islamic insurance demand. [102] Abdullah found a positive but insignificant impact of education on demand for life insurance

[97] Waheed Akhter and Saad Ullah Khan, "Determinants of Takāful and Conventional Insurance Demand: A Regional Analysis," *Cogent Economics & Finance* 5, no. 1 (2017/01/01 2017), http://dx.doi.org/10.1080/23322039.2017.1291150.

[98] Z.A. Rahman, M.Y. Rosylin, and A.B. Faizah, "Family TakāFul: It's Role in Social Economic Development and as a Savings and Investment Instrument in Malaysia–an Extention," *Shariah Journal* 16 (2008)..

[99] H Redzuan, Z.A. Rahman, and S Aidid, "Economic Determinants of Family TakāFul Consumption: Evidence from Malaysia," *International Review of Business Research Papers* 5 (2009).

[100]H Redzuan, Z.A. Rahman, and S Aidid, "Economic Determinants of Family TakāFul Consumption: Evidence from Malaysia," *International Review of Business Research Papers* 5 (2009).

[101] Hawariyuni Weni and Salleh Marhanum Che Mohd, "Modeling the Demand for Family and General Takaful in Malaysia (a Comparative Study): Ardl Approach to Cointegration," *Tazkia Islamic Finance and Business Review* 7, no. 1 (2012).

[102] M. Sherif and N. A. Shaairi, "Determinants of Demand on Family Takaful in Malaysia," *Journal of Islamic Accounting and Business Research* 4, no. 1 (2013).

and Family Takaful.[103] Redzuan, in his study analyzing Malaysian life insurance and Family Takaful from period 1970–2008 using ARDL approach, found a significantly positive and long run impact of education level on life insurance and Family Takaful demand.[104] Islamic insurance is even more limited in highly educated people according to Akhter & Hussain.[105] Altogether, education might not be considered a true measure and proxy for awareness of Islamic insurance.

Likewise, Akhter, Khan and El-Gammal conduct a parallel study between conventional insurance and Islamic insurance by using similar determinants. They also compile all existing literature of Islamic insurance. They observe 33 countries worldwide where both Islamic insurance and conventional insurance operators exist. They conclude:

> For conventional insurance demand, income, urbanization, financial sector developments, inflation and education are the significant factors, while for Islamic insurance demand, inflation, income, education, urbanization and dependency ratio are significant factors affecting their relative demand. For the ASEAN region, income, urbanization, and financial sector developments have significant positive impact for both insurance and Islamic insurance demand but dependency ratio shows negative impact. Inflation shows positive impact for Islamic insurance demand while negative impact on insurance. In case of Middle East region, income, inflation and urbanization shows positive impact on both products demand while dependency reveals negative impact. Education shows positive triggering insurance demand while affecting negatively to Islamic insurance demand due to due to lack of its awareness.[106]

From that observation, it can be inferred that the very similar domestic factors influencing for conventional insurance demand are also responsible for the development of Islamic

[103] N. I. Abdullah, Analysis of Demand for Family Takaful and Life Insurance: A Comparative Study in Malaysia, *Journal of Islamic Economics, Banking and Finance*, 68 Vol. 8 No. 4, Oct – Dec. (2012). N. I. Abdullah, "Analysis of Demand for Family Takaful and Life Insurance: A Comparative Study in Malaysia," *Journal of Islamic Economics, Banking and Finance* 8, no. 4 (2012).

[104] H. Redzuan, "Analysis of the Demand for Life Insurance and Family Takaful " (paper presented at the Australian Academy of Business and Social Sciences Conference2014), https://www.aabss.org.au/system/files/published/AABSS2014_290.pdf. . H. Redzuan, H., 'Analysis of the demand for life insurance and family Takāful (Working paper)', *Australian Academy of Business and Social Sciences Conference* 2014. Paper is retrieved from https://www.aabss.org.au/system/files/ published/AABSS2014_290.pdf.

[105] Waheed Akhter and T. Hussain, "Takaful Standards and Customer Perceptions Affecting Takaful Practices in Pakistan: A Survey," *International Journal of Islamic and Middle Eastern Finance and Management* 5 (2012). http://dx.doi.org/10.1108/17538391211255214.

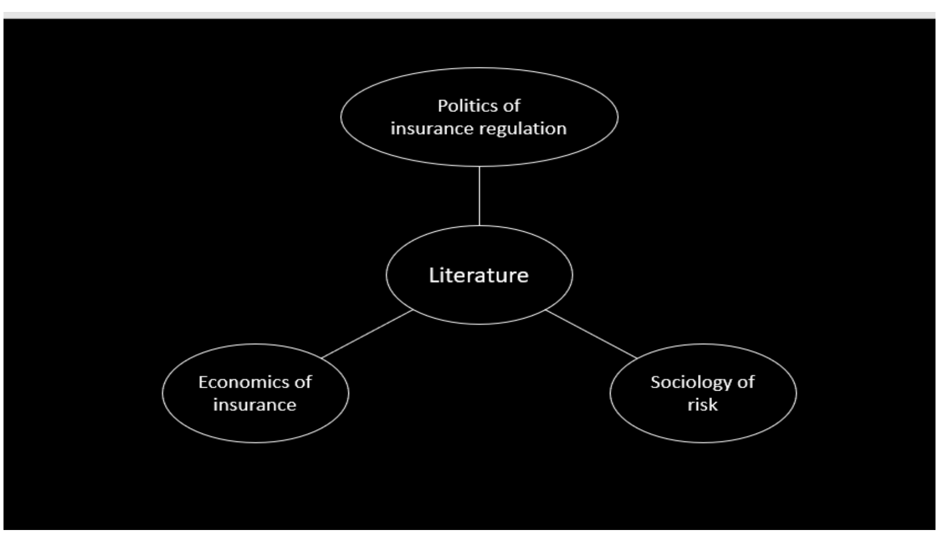
[106] Akhter and Khan.

insurance. A possible explanation for this similarity is because Islamic insurance, despite its initial intention of being alternative insurance, still needs similar conditions to grow.

Altogether, previous studies on insurance and Islamic insurance have provided various useful explanations for the national demand of Islamic insurance. However, almost all of them consider these financial services develop in an institutional, historical, and cultural-absent space. Those factors are unable to fully account for variation in Islamic insurance development among the three countries included in this study. In addition, these countries have many commonalities in these factors. Moreover, Akhter, Khan and El Gammal suggest that literature on Islamic insurance are lack of discussion on its institutional and political factors. According to them, 'future studies could be conducted using insurance and Islamic insurance product lines (life or nonlife insurance with family or general Takaful) considering the global financial crisis, institutional and political factors impact on their demand'. Without dismissing these findings, there is an urgent need to understand Islamic insurance development in a more comprehensive manner. Islamic insurance is designed as a private-based mechanism, but its development has been shaped by political, legal, institutional, and cultural limitations of the country.

The figure below shows the current state of study on Islamic insurance. Most of the study are focusing on the economic determinants of Islamic insurance. Meanwhile, the discussion on its politics and social aspects of Islamic insurance is quite scarce.

Figure 2-1: Summary of the Current Scholarship on Islamic Insurance



Islamic insurance as a political product

The existence of the global financial crisis is part of an international environment that can be influential in the development of Islamic insurance. According to Ercanbrack, the process of producing Islamic finance law, products and services illustrate complex fields of action driven by power dynamics, neoliberal paradigms and the institutional momentum of the global economy.[107] The timing of Islamic insurance establishment in a country can be decisive for its development. As a global service, insurance needs global linkage in order to grow. This is the environment where the company can re-invest and gain capital. Some of the Islamic insurance companies have managed to develop sophisticated Islamic re-insurance portfolios that sustain their development.[108] This statement shows that political institutions are a vital element in the development of Islamic insurance.

Political coalition formation

In *Fragile by Design: The Political Origins of Banking Crises & Scarce Credit,* Charles Calomiris and Stephen Haber argue that the modern Banking arrangements are 'not a passive response to some efficiency criterion but rather the product of political deals that determine which laws are passed'. [109] They provide a rich history of banking over the last couple of centuries to convince us that banking instability has its roots, not in any fragility inherent to commercial banking, but in deals struck between governments and various interest groups. The book discusses the question of why banking systems are unstable in so many countries, but not in the others. For instance, the United States has had twelve banking crises since 1840, while Canada has had none. Economists have been developing models to explain those crises. Banking performance is shown in two indicators: credit abundance and the propensity of crises. They understand that the monopolization of banking will tend to result in reduced supply credit, which leads to low banking performance and decreases prosperity. Nonetheless, the models cannot explain why such a system of monopolized banking would arise in some countries.

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[107] Ercanbrack.
[108] Abdulrahman Khalil Tolefat and Mehmet Asutay, *Takaful Investment Portfolios : A Study of the Composition of Takaful Funds in the Gcc and Malaysia* (New York: New York: John Wiley &amp Sons, Incorporated, 2013).
[109] Calomiris.

According to them, the banking performance of a country is related to the bargaining process within the banking system or so-called the Game of Bank Bargains. It is a strategic interaction between the government and private sectors. The game operates according to the logic of politics, not the logic of efficiency. The game governs entry and competition, the pricing of credit and its terms, and the allocation of losses when banks fail. Who is in the partnership varies across countries and within countries over time--because who else is in the partnership depends on who is politically crucial?

Three political realities shape this bargaining game. There is active encouragement of the government, the political coalition in charge of banking policy, and regulatory framework. Successful banking cannot develop without government support. For instance, if the government is lacking the desire to allow a competitive environment to flourish due to fiscal needs, the banking system will be repressed. On the contrary, as in England before 1820s, the government permitted a competitive bank system to develop thus, created a stable system with an abundance of credit available for private sectors. Bank crises can happen in autocracies and populist democracies. It is not the political system per se, but what kind of political coalition designs the country's banking system. Crises occur in the countries with political coalition 'that is willing to tolerate instability as the price for obtaining the benefits that it extracts from controlling banking regulations.'[110]

Moreover, the discussion on regulations should focus on the outcome of the regulations. It should not focus on whether the institution needs more or fewer rules or regulations. Some countries create more regulations but facilitate better market outcome, while others initiate deregulation that ends up at market failure.

The domestic institutional arrangement especially the insurance regulation is crucial for Islamic insurance development. Meier suggests insurance regulation is similar to other forms of regulation, that it is inherently a political process whereby political actors seek to allocate the powers of the state for their benefit. Furthermore, he identifies four major political actors (or sets of actors) in the literature: the regulatory agency (i.e., the insurance commission), the regulated industry (in this case the insurance industries), non-industry interests (primarily though

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[110] Ibid.

not exclusively in this case consumer interest groups), and political elites (legislators, chief executives, federal officials, et. al.) [111]

The political elites are particularly crucial within Muslim societies throughout history. Nonetheless, the support from the political elites or government does not always give a positive impact on Islamic insurance development. Calomiris and Haber have shown in the case of the banking system that the issue is on how and what support the government provides.[112]

However, a single political actor cannot determine the development of Islamic insurance in a country. Islamic insurance development is a result of the interaction of different political actors. Therefore, Islamic insurance flourishes when there are institutional support and regulatory framework as a product of the coalition among the political actors involved.

The scholars of State-Society relations elaborate on the interactions between the state institutions and societal groups to negotiate how public authority is exercised and study how people can influence it. They consider states and societies are both mutually dependent and mutually constitutive.[113] The following paragraphs explain the relevance of state-society scholarship with Islamic insurance.

Islamic insurance developed within a broader popular demand for Islamization or Islamic revivalism. The 1979 revolution in Iran had an enormous global effect. It was for the first time Islamists gained power in a modern state. This event coincided with, and some have argued spurred, a broader resurgence of Islam around the world, including in these three countries.[114] Abbot defines Islamization as 'the intensification of Islamic influence on social, cultural, economic and political relations.'[115] There was an increasing commitment toward Islam among the middle classes in these countries. The state has a range of options from to co-opt, to accommodate, and

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[111] Kenneth J. Meier, "The Politics of Insurance Regulation," *The Journal of Risk and Insurance* 58, no. 4 (1991), http://dx.doi.org/10.2307/253081.
[112] Calomiris, *Fragile by Design the Political Origins of Banking Crises and Scarce Credit*.
[113] Marc, A., Willman, A., Aslam, G., and Rebosio, M., with Balasuriya, K., 2013, 'Understanding state-society connectedness'. Chapter 2 in Societal Dynamics and Fragility. Engaging Societies in Responding to Fragile Situations. World Bank, Washington, D.C.
[114] John L Esposito, *Islam and Politics*, 4th ed.. (Syracuse, N.Y.: Syracuse, N.Y. : Syracuse University Press, 1998).page 309–310.
[115] Abbott and Gregorios-Pippas.

to repress those demands. Furthermore, this state-society relations framework provides us with a deeper understanding of how incentive is generated, and legitimacy is acquired by the state.

The nature of the political settlement can greatly affect upon state-society relations. In many fragile and conflict-affected states, relations are based on patronage and lack of accountability. The prominence of informal institutions and relationships and unofficial processes result in divergences between formal systems and rules and actual practice. As we will see in the case study of Pakistan, the Pakistani political elites, who benefit from patronage and income from natural resource rents and criminal activities, often have little incentive to engage with citizens and to build effective public authority. The concentration of power in a few elites also limits the participation of citizens from public life. In some situations, citizens may be excluded from public life through state repression and violence. This results in a legacy of negative and weak state-society relations. Efforts to promote an inclusive political settlement can re-shape relations and contribute to political and social transformation. Moreover, to understand the reason for the elites to support or reject Islamic insurance, we need to put greater attention to questions of power and altering elite incentives.[116]

The country's fundamental political institutions structure the complex bargains made between various groups within each country polity. This understanding leads us to the concept of path dependence. Path dependence is the idea that decisions we are faced with depending on past knowledge trajectory and decisions made and are thus limited by the current competence base. In other words, history matters for current decision-making situations and has a strong influence on strategic planning.

Institutional economics

Institutional economics would argue that the emergence of Islamic insurance or any contemporary economic models could be explained from the institutional evolutionary process within certain society in the past. Specifically, on insurance, the transformation of uncertainty into risk marked the final shift of primitive/traditional exchange into a modern system.

[116] Huma Haider, "State-Society Relations and Citizenship in Situations of Conflict and Fragility," (September 2011), http://www.gsdrc.org/docs/open/con88.pdf.

Accordingly, the process is influenced by the interaction of the intensity and extensity of economic activity (capital), innovations, and the role of a political institution or the state.

Institutional economists develop analytical frameworks specifically to explain the influence of institutions on economic performance through long periods of time. According to them, the current forms of political, economic, and even military organization are derived from the opportunity set provided by the institutional structure that evolved incrementally. This idea is often called path dependence. Moreover, institutions are the key to understand how people make choices under conditions of (economic) uncertainty and ambiguity. Therefore, by using that approach, this section elaborates variables derived by this school of thought that shape institutional structure of risk.

Their works started by questioning the rationality postulate of the neoclassical model. They argue people do not determine their choices directly through an elaborate rational process. Rationality cannot sufficiently answer why people make the choices they do. Admittedly, that model explains clearly the options and tradeoffs people have, but at the same time people are also facing difficulties in deciphering their complex circumstances. There are constraints preventing people from choosing the best response. Indeed, they need ways to reduce uncertainty and to create order in human interaction.

Likewise, a simple cost-benefit analysis cannot satisfactorily explain the way people choose the strategy against economic insecurity.[117] As mentioned above, an ideology such as the religious prohibition of commercial insurance is partly responsible for the low insurance penetration in Muslim majority countries and the emergence of Islamic insurance. In other words, it gives constraint for people to choose specific strategy. Therefore, we need an analytical framework which incorporates an understanding of how ideologies and ideas determine the choices people made in responding to an economic situation.

Thorstein Veblen, a Norwegian-American economist and sociologist, laid the foundation for the development of American institutional economics through his criticism on the traditional static economic theory. Influenced by Darwinism, he added historical and evolutionary processes

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[117] Douglass C. (Douglass Cecil) North, *Institutions, Institutional Change, and Economic Performance* (Cambridge: Cambridge, 1990).

to economic analysis. According to him, the economy is embedded in social institutions, therefore it should not be treated as an autonomous and static entity. Evolutionary process and institutions have significant roles in shaping economic behavior. This perspective enables economists to explore economic problem as part of broader socio-cultural development and to consider the economy as an evolving entity of bounded rationality.

Veblen defines institutions as both units of evolutionary selection and repositories of knowledge. But rather than being the determinant factor of the individual action, institutions develop in the process of coevolution with the other. In other words, the economy can be considered as the locus for dynamic interaction between the individual as agency and institutions as social structure.

In 1904, he published *The Theory of Business Enterprise*, where he utilized evolutionary principles to explain the development of new industrial processes in America at the time. He saw them because of the growth of industrial processes in the context of small business firms that had evolved earlier to organize craft production. Veblen's institutionalism was a central element of American economics during the interwar period post-1919, but then it never managed to take hold due to mostly the emergence of positivism within social sciences and also due to the misused of principles of biological evolution to justify racist, sexist and imperialistic practices, such as the Nazis. [118]

Since the 1960s, several scholars have been tried to refine the institutionalist approach in the understanding the economy. Rather than merely criticizing neoclassical economy, it builds on, modifies and extends it. This approach, so called New Institutional Economics, incorporates a theory of institutions into economics. What it means is the approach retains and builds on the fundamental assumption of scarcity and hence competition - the basis of the choice theoretic approach that underlies microeconomic.[119] One of the influential scholars in this school is the 1993 Nobel laureate, Douglass North.

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[118] Geoffrey M. Hodgson, *The Evolution of Institutional Economics: Agency, Structure and Darwinism in American Institutionalism*. London and New York: Routledge, 2004.
[119] Most scholars view the work of Ronald Coase (Ronald Coase (1960), The Problem of Social Cost, Journal of Law and Economics 3:1-44) as a central inspiration for the field. To get a complete list of scholars of the New Institutional Economics, see Alexandra Benham, "New Institutional Economics: Glossary," New Institutional

In his 1991 journal article *Institutions*, he describes how innovations in systems of exchange, long-distance trade in early modern Europe from the 11th to the 16th centuries enabled Europeans to transform the tribal system of exchange into a sequentially more complex organization that eventually led to the rise of the Western World. Those innovations include techniques and methods to evade usury laws and actuarial science that are crucial for transforming society into the modern capitalistic economy.[120]

The institution evolution started within tribal or village community in which people relied heavily on a dense social network. People have an intimate understanding of each other; therefore, they were able to create, for instance, pool resources out of mutual trust and the threat of collective violence (punishment) for preserving order. Although the societal cost in this tribal or village is very high, it will not create additional transaction cost. As of the economic interaction is expanding beyond village or tribal community and become a regional exchange, the dense social network is replaced by more infrequent clientization of the players. Typically, there is no central political authority governing this regional network. Instead of a unified political structure or formal rules, religious precepts-imposed standards for players' behavior. The religious precept of "thou shalt not defect" acts as a paternalistic divine command that enables people from diverse geographical backgrounds but embracing the same religion cooperate. The next stage shows economic exchange becoming more complex, therefore impersonal and kinship ties, a voluntaristic constraint such as the religious rulings, and other informal mechanisms are no longer effective. Coercive political order and judicial organizations are needed in an age of capital markets and manufacturing firms.[121] Arguably, the increase in the volume of trade is partly responsible for this evolution process. It necessitates the society to find ways to lower the transaction cost to achieve what so called economies of scale.

The term 'partly' above means that volume of trade cannot be the only cause. In fact, many societies have developed differently. After centuries, certain society relies more on formal

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Economics: Glossary, accessed March 12, 2017, https://www.coase.org/nieglossary.htm#REFNewInstitutionalEconomics.

[120] Douglass C. North, "Institutions." *The Journal of Economic Perspectives* 5, no. 1 (1991): 97-112. http://www.jstor.org/stable/1942704.

[121] North, *Institutions, Institutional Change, and Economic Performance*.

mechanisms while others still maintain the use of informal ways. Douglass North examines the differences between *Suq* (Bazaar economies engaged in regional trade) which has existed for thousand years and still exists nowadays in North Africa, the Middle East, and the modern market of Western World in order to illustrate different paths of development. The question is; what factors make the difference?

Suq is characterized by widespread, relatively impersonal but clientized exchange, and relatively high costs of transacting. It is widespread because it consists of a multiplicity of small-scale enterprises, low fixed cost, and an enormous number of small transactions. It is not based on kinship ties, but nonetheless, it is still based on face-to-face contacts where trading involves a continual search for specific partners (clientization). There is no institution specifically for distributing market information and at the same time, there is a minimal and decentralized governmental control. The transaction is performed by raising the costs of transacting to another party to exchange. People are seeking gains at the expense of others. In this context, one makes a profit by relying more on having better information and bargaining skills than one's adversary.[122]

Information asymmetries make regional trade of Suq inefficient. Based on the previous generic model, it is expected that there would be an evolution of voluntary organizations. The organizations then would be able to reduce uncertainties and mitigate any upcoming hazards due to the asymmetries. On the contrary, these voluntary organizations are missing in the Suq system due to the lack of innovations in legal institutions and juridical enforcement, which make the organizations viable and profitable. As a result, there is no incentive to alter the system.[123]

North argues that the modern market of the Western World was created not only because of the expansion and because of the enormous number of trade transactions. Some innovations enabled them to lower transaction cost.

> These innovations occurred at three cost margins:(I) those that increased the mobility of capital, (2) those that lowered information costs, (3) those that spread risk. For instance, European created innovations in the form of techniques and methods to evade usury laws

[122] Douglass C. North, *Institutions, Institutional Change, and Economic Performance* (Cambridge: Cambridge, 1990), page *124.*
[123] Ibid.

> that later enhanced the mobility of capital. From 11th to the 16th centuries, European created innovations that enhanced the mobility of capital were the techniques and methods evolved to evade usury laws. The variety of ingenious ways by which interest was disguised in loan contracts ranged from "penalties for late payment," to exchange rate manipulation, to the early form of the mortgage; but all increased the costs of contracting. The costliness of usury laws was not only that they made the writing of contracts to disguise interests complex and cumbersome, but also that enforceability of such contracts became more problematic. As the demand for capital increased and evasion became more general, usury laws gradually broke down and rates of interest were permitted. In consequence, the costs of writing contracts and the costs of enforcing them declined.[124]

Another innovation to increase the mobility of capital was the development of techniques and instruments of discounting methods[125] along with development of the centers that could specialize in that-such as the Champagne fairs, then banks, and finally financial houses. This method enabled people to develop credit by which increased the mobility of capital. Moreover, the standardized system of accounting is also important for maintaining control of agents involved in long-distance trade. Previously, people relied more on kinship and family ties to do that. Accounting system and notarial records provides an evidence-based mechanism to monitor trade transaction. It is different to the tribal/traditional mechanism which relies more on agency or witness. Adding to that, information cost was lowered through printing of prices of various commodities as well as the materials containing information on weights, customs, brokerage fees, postal system, and exchange rates.[126]

The transformation of uncertainty into risk marked the final transformation of the primitive/traditional exchange into a modern system as previously discussed in the section of 'insurance: and institutional history'. Actuarial science enables people to convert uncertainty into risk and thereby reducing the costs of the transaction through the provision of a hedge against variability.[127] As the economy grew, there was a need to pool huge capital in financing risky

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[124] North, "Institutions".

[125] Discounting is the process of determining the present value of a payment or a stream of payments that is to be received in the future. Read more: Discounting Definition | Investopedia http://www.investopedia.com/terms/d/discounting.asp#ixzz4cifq8uxK

[126] North*, page 126.*

[127]Ibid.

business activities. Besides the development of actuarial science, the *commenda* was developed as an institution that permitted a large number of investors to engage in a new venture. [128] The commenda itself was originated from Jewish, Byzantine, and Muslim traditions that later developed by Italian merchants to English regulated company. It was promulgated by The Marine Insurance Act 1743 and became the first commercial insurance of the modern economy.

In the later development, transfer risk mechanism of insurance is not only used for risky activities but almost on all economy. The market can transfer risk to institution or people who can handle risk effectively. For instance, the cost of rebuilding house due to environmental disaster is beyond individual's capacity, but by buying insurance premium the individual can let insurance company with many properties and shareholders, to manage that loss efficiently.

It is also crucial to mention the innovation in the form of legislation to 'distinguish' speculation and gambling. One of the major issues was the close relationship between insurance business, future trading and gambling. Even an economist, John Kay argues that the whole of capitalism is based on gambling. A speculative investment that led to several contemporary economic crises is not something that is unusual. Speculation is the main feature of the modern economy.[129] Following the enactment of the Marine Insurance, Sir John Barnard's Act of 1743 states that the 'evil practice of compounding or making up differences to the great discouragement of industry, and to the manifest detriment of trade and commerce.[130] Of course, the controversy of gambling and speculative investment was not over. It is part of the contemporary debate. Nevertheless, the legislation had enabled capital markets to grow. People had no hesitation to put their money in investments despite how speculative they are because they were convinced that it was not gambling.

As a side note, it is important to put aside our normative judgment in discussing these two types of institutions. Exchange in Suq or even in tribal or village communities is not simple and always inferior compares to the modern market. It is inefficient, but arguably, that is the best

[128] Commenda is the origin 'risk transferring' of the joint stock company. Read further: Gene W. Heck, *Charlemagne, Muhammad, and the Arab Roots of Capitalism* (Walter De Gruyter, 2006).
[129] John Kay, "Gambling Is a Feature of Capitalism-Not a Bug," *Prospect Magazine*, 14 March 2017.
[130] Pat O'Malley, *Risk, Uncertainty and Government* (Portland, Oregon: GlassHouse, 2004), page 103.

way considering the local circumstances. It happens because there is an incentive or disincentive for the society to develop certain mechanisms.

The innovations on contract monitoring and enforcement such as accounting method, notarial records, and merchant organizations would not be sufficient to create an efficient capital markets without enforcement by the state. The state was the major player because there was continuous link between the fiscal needs of the state and its relationship with merchants and general citizen. North uses the comparison between the state that encourage innovations during the evolution of the modern market such as the Netherlands and England, and the empires in decline Spain and Portugal. The main difference was the declining empire set up a centralized system that generated rent-seeking behavior while the Netherland and England created a more decentralized system that encouraged check and balance. For instance, the establishment of Bank of England and a fiscal system in which expenditures were tied to tax revenue in England had laid the ground for both a healthy financial basis for government and the development of private markets. Acemoglu and Robinson use terms of extractive and inclusive institutions. The extractive institutions hamper or block economic growth while inclusive are the ones do not. For them, how a political institution is designed is the key to the success or failure of the nation.[131] Altogether, the ability of the state to restrain itself for not confiscate assets or using its coercive power to increase uncertainty in the economy made it possible for evolution of the modern market.[132]

Deriving from North's explanation on these several institutional structures, we can identify that there are three variables involved in the evolution of institution. An institution is evolved primarily from "interplay between two fundamental economic forces: the economies of scale associated with a growing volume of trade, and the development of improved mechanisms to enforce contracts at lower costs. The causation runs both ways. The increasing volume of long-distance trade raised the rate of return to merchants of devising effective mechanisms for enforcing contracts. In turn, the development of such mechanisms lowered the costs of contracting and made trade more profitable, thereby increasing its volume." Nevertheless, it is

[131] Daron Acemoglu and James A. Robinson, *Why Nations Fail: The Origins of Power, Prosperity, and Poverty*, 1st ed. (New York: Crown Publisher, 2012).
[132] North, Institution, Institutional Change and Economic performance…, page 129.

not the whole story. The state is crucial in ensuring this process runs without experiencing disruption, either due to external factors or more importantly from the state itself.[133]

As mentioned before, the prevalent cooperative practices in both personal and business life of the Muslim societies substantially reduce the need for insurance – a society is expected to take care of those in need. This may be why insurance was not introduced in the original Islamic Empire, despite the existence of an extensive global trade network.[134]Besides that, the decline of trade and 'the absence of state' within the Islamdom during the European colonization probably had a role in it too.

It seems there was no incentive for Muslim societies to develop institutionalization of risk beyond kinship based common pool resources. The information on individual moral characters and skills seem more important than generating data to calculate risk. Actuarial science did not develop and shape the way the Muslims deal with economic insecurity within this society. The development of probabilistic thinking as the essence of the innovation of actuarial science possibly the most important key to understanding the difference. The development of probabilistic thinking depended on the Enlightenment's rejection of argument from authority and the diminished influence of religious doctrine.[135] It is expected that probabilistic thinking in the modern sense would not develop in a society where religious authority or tradition is still intact. Therefore, it is interesting how contemporary Muslim societies integrate it into the construction of Islamic insurance.

Overall, institutional economics' approach suggests that the emergence of Islamic insurance or alternative insurance, in general, should be explained not only from its contemporary development but also more importantly how the past specifically its historical evolution influences its current emergence. Arguably, those variables compose a path dependence, which provides constraints for people choosing the best response against their economic insecurity.

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[133] Ibid.
[134] Zaman, "Islamic Economics: A Survey of the Literature."
[135] Kay.

Islamic insurance as a social practice

How do people respond to economic insecurity- illness, unemployment, 'widowhood', and old age? Moreover, if commercial insurance, the 300 years old industry with the gross contribution (gross premiums) of $4.6 trillion (2014),[136] can be considered as the most efficient way to do that, what makes people choose other strategy over this? In a traditional society, they relied mostly on family support and social networks in coping with these unforeseen events. For instance, peasants created collective rice barn as a type of insurance at the time of crop failure or natural disasters. Afterward, modern society considered this informal mechanism insufficient. It is because the nature of modern insecurity or so-called risk is different from the previous one. There are some theories inform people attitude toward insurance.

Social action

One theory is theory on social action. The social action theory by Max Weber explains that human actions are meaningful and that certain reasons push people into various kinds of actions. To Weber, there are three kinds of action: traditional (based on customs and habits); affective (based on the emotional state of the individual at a particular time); and rational (based on a clear awareness of a goal).[137] This also implies that certain factors tend to influence one's behavior toward insurance. People might choose to prefer insurance due to intuitive or cultural underpinnings. On the other hand, people can rationally decide to have an insurance policy for clearly economic reasons.

The social action theory also suggests that there is a societal factor for the development of Islamic insurance services. Islamic insurance is a private-based service and not a social insurance because the state is not the one who provides the services. Therefore, an Islamic insurance company needs to be able to convince the consumers to buy it.

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[136] Insurance Information Institute, *World Insurance Factbook 2015"World Overview,"* (2016), http://www.iii.org/publications/international-insurance-fact-book-2016/world-overview., accessed January 22, 2017, and Middle East Global Advisors (MEGA), *World Takaful Report* (2016), http://www.takaful.coop/images/stories/WTR%202008.pdf accessed January 22, 2017.

[137] Max Weber, *Economy and Society*, vol. 1 (Berkeley: University of California Press, 1924).

Support from the Muslim population in the societal level is also important for its development, along together with its political dynamic in the state level. Moreover, it is not only the support toward the product but also the support toward the agency, which provides it. As private sector or market[138] has become the dominant agency of Islamic finance recently, a positive attitude toward the private sector from the population will be crucial for Islamic insurance to flourish in the country. In addition, the middle class has always been essential for the acceptance of any type of reform, either in the form of radicalism of Islamic state or modernism such as Islamic insurance.

According to Charles Tripp, the reliance on the private sector has been one of the dilemmas in the Islamization of the economy in general. Islamic insurance was intended as an alternative of conventional insurance, but then it could not escape from the existing paradigm of market capitalism.[139] Consequently, Islamic insurance tends to be more developed in capitalistic countries where there is high support for the private sector and market mechanism.

Also, economic modernization and globalization have created a new global Islamic identity, which defines an individual's preference on using Islamic insurance. The more global a Muslim is, the more likely this individual to embrace Islamic financial services.[140] Timur Kuran argues the real purpose of Islamic economics has not been economic improvement but cultivation of a distinct Islamic identity to resist cultural globalization. Based on his literature survey, Islamic banking differs from conventional banking mainly in symbolism and terminology. [141] The Islamic sub-economies that have sprung up across the Islamic world are commonly viewed as manifestations of Islamic economics. In reality, Kuran demonstrates, they emerged to meet the economic aspirations of socially marginalized groups. The bottom-up process of Islamic economics in Indonesia is an instance of this phenomenon. The Islamic enterprises that form

[138] Tripp.
[139] Ibid.
[140] Mark Smyth, "Islamic Finance in an Almost Postcrisis and Postrevolutionary World: As in Politics, All Islamic Finance Is Local," in *Contemporary Islamic Finance: Innovations, Applications, and Best Practices*, ed. Karen Hunt-Ahmed (New Jersey: John Wiley & Sons, Inc., 2013).
[141] Timur Kuran, "Islam and Economic Performance: Historical and Contemporary Links," *Journal of Economic Literature* 56, no. 4 (December 2018): 1292–1359, https://doi.org/10.1257/jel.20171243.

these sub economies provide advancement opportunities to the disadvantaged. By enhancing interpersonal trust, they also facilitate intragroup transactions.[142]

Furthermore, several ethnographic studies on Islamic business networks documented by Timur Kuran show various non-economic motivations for members joining the networks. The first is that network membership is akin to belonging to a club. Members receive support from other members in return for contributions to the group and, sometimes, to the wider society as well. For instance, the members of the global Hizmet network led by Fethullah Gülen, Syria's Damascus-based Jamaʻat Zayd, the Bilal Muslim Mission of sub-Saharan Africa, or Eastern Indonesia's Hadhrami network coordinated by the Islamic organization Al-Khairaat, give each other business, and they support one another financially in times of need. In return for these advantages, they help to finance the group's activities and participate in its recruitment campaigns. Their economic interactions are embedded in deeper social and cultural relations. They also provide charity, both on their own and jointly with the group. Thus, the members of Jamaʻat Zayd finance mosques, schools, and hospitals affiliated with the group. They also fund poverty alleviation programs, provide care for orphans, and help impoverished youths get married.[143] Spending some of their profits for helping others bring them many benefits. This generous gesture is considered as an integral part of their economic activities. Through its members' donations, the Hizmet movement has established schools in 130 countries, along with thousands of mostly volunteer-staffed outreach centers.[144]

Secondly, Islamic networks benefit from alliances with politicians who give them access to rents. In providing social services, the Gülen network has also pursued political power in its homeland, Turkey. During the first decade of Islamist rule in Turkey under the Justice and Development Party (AKP), Gülen's network shared in the privileges of power, including preferential treatment in government hiring and contracts. [145] These mixed motivations exist and

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[142] Kuran.
[143] Timur Kuran, "Islam and Economic Performance: Historical and Contemporary Links," *Journal of Economic Literature* 56, no. 4 (2018/12// 2018), http://dx.doi.org/10.1257/jel.20171243.
[144] Anwar Alam, *For the Sake of Allah: The Origin, Development, and Discourse of the Gulen Movement* (New Jersey: Blue Dome Press, 2019).
[145] Kuran.

compete against each other as part of popular support over the development of Islamic insurance.

In line with arguments above, the scholars of insurance have pointed out the significant of religion and culture in consumer's decision of buying insurance. Treerattanapun shows empirical results of how consumers may respond to insurance solicitations according to their cultural belief, not only economic rationality.[146] For example, the prohibition of conventional insurance by Islamic law is often used as the explanation for the low insurance demand in the Islamdom. Insurance markets even in the most developed Muslim-majority countries are largely at nascent or growth stage of development. Studying several Muslim majority countries, Rahmane (2009) and Yazid et al. (2012) find that the determinants of Islamic life insurance are like those of conventional life insurance on all points except religion. According to them, religion plays significant role in encouraging Muslim population to take Islamic life insurance because this type of insurance is considered consistent with Islam.[147]

Furthermore, by using a regression analysis in 1980 and 1987, Browne and Kim investigate the factors that lead to variations in the demand for life insurance across countries. They report a negative correlation between the demand for life insurance and Muslim countries.[148] Also, based on a study of 45 developing countries, Outreville finds that personal income, inflation, and the development of the country's financial sector have the most important impact on the demand for life insurance. In line with Browne and Kim's study, the author reports that in Muslim countries, the demand for life insurance and Muslim religion are negatively correlated.[149]

However, other researchers emphasize on the characters and attitude of the religion or culture, rather than on the religious doctrine of the religion itself. Chui and Kwok (2009) using Hofstede's cultural dimensions, and data from 1976–2001 across 41 countries. They argue that

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[146] Aranee Treerattanapun, "The Impact of Culture on Non-Life Insurance Consumption," *Wharton Research Scholars* 78 (2011).
[147] Z. A. Rahmane, "Takaful: Potential Demand and Growth," *J.KAU: Islamic Econ.* 22, no. 1 (2009). And A. S. Yazid et al., "Determinants of Family Takaful (Islamic Life Insurance) Demand: A Conceptual Framework for a Malaysian Study," *International Journal of Business and Management* 7, no. 6 (2012).
[148] Mark J. Browne and Kihong Kim, "An International Analysis of Life Insurance Demand," *The Journal of Risk and Insurance* 60, no. 4 (1993).
[149] J. François Outreville, "Life Insurance Markets in Developing Countries," *The Journal of Risk and Insurance* 63, no. 2 (1996 1996), http://dx.doi.org/10.2307/253745.

culture with strong individualism indeed has a significant, positive effect on life insurance consumption. People with a culture with emphasis on independence and autonomy tend to rely more on market life insurance and less on social network security (financial help offered by fellow kinsmen to one's dependents upon one's death) than people with culture of interdependence or collectivism.[150]

Other scholars do not consider religion or culture as a socio-demographic characteristic at the country level, but at the personal/individual level (i.e. at the consumer level). Muslims might have different interests in Islam (as a faith/religion) or attribute a different importance to it in their lives. Thus, they may expect that Muslims vary in terms of their Islamic beliefs, and that their behaviors and attitudes will depend accordingly. For example, Souiden and Jabeur argue that the higher (lower) the Islamic beliefs of individuals, the less (more) favorable their attitude will be toward conventional life insurance and the more (less) favorable their attitude will be toward Islamic life insurance.[151]

In addition, Stasavage and Scheve provide an interesting study on religiosity and social insurance. They argue individuals who are religious will prefer lower levels of social insurance than will individuals who are secular. To the extent policy outcomes reflect individual preferences, then countries with higher levels of religiosity will have lower levels of welfare state spending.[152]

Informal economy

Besides a theory on the growth of Islamic insurance, we also need theory on the lack of its development. The literature on informal economy suggest that market failures responsible for the existence of economic activities outside the formal economy. Market failures in the form of regulation constraint, tax evasion, state’s weaknesses, economic crises or conflict have made people take alternatives. It is not because of the path dependence as suggested by institutional

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[150] Andy C W Chui and Chuck C Y %J Journal of International Business Studies Kwok, "National Culture and Life Insurance Consumption," 39, no. 1 (January 01 2008), http://dx.doi.org/10.1057/palgrave.jibs.8400316.
[151] Nizar Souiden and Yosr Jabeur, "The Impact of Islamic Beliefs on Consumers’ Attitudes and Purchase Intentions of Life Insurance," 33, no. 4 (2015), http://dx.doi.org/doi:10.1108/IJBM-01-2014-0016.
[152]D. Stasavage and K. Scheve, "Religion and Preferences for Social Insurance," *Quaterly Journal of Political Science* 1 (2006).

economics, but more of the current events that disrupt the efficiency of the market. It means even a highly modern society can roll back to informal in certain circumstances.

Islamic insurance has been presented as an alternative to conventional insurance. However, Islamic insurance is built on a similar platform, which is a formal and private-based scheme of insurance. After almost four decades of the introduction of Islamic insurance, the demand for Islamic insurance is still considered very low. The literature on informal economy might help us to understand why many Muslims are still reluctance in using the modern scheme of Islamic insurance and maintaining their informal ways to deal with economic hardships.

During the 1950s and 1960s, many economists believed that low-income, traditional, subsistence, and informal economies of developing countries could be transformed into dynamic modern, capitalist, wage-employment, formal economies through a combination of correct economic policies and enough resources: capital, plentiful labor, and technology. As the countries gaining more economic growth or industrial development, the labor forces from the informal economy will be absorbed by the modern sector, which offers higher wages.

Many models including the dual-sector or the Lewis model, which was invented by an economist W. Arthur Lewis in 1954, describe this process. The model assumes that the developing country has a surplus of unproductive labor especially from agricultural sector. This assumption is based on the classical economy's argument such as Adam Smith who argued before that unlimited supply of labor was available at subsistence wage. Later, these workers become attracted to the manufacturing sector where higher wages are offered. At the beginning, due to the 'unlimited' supply of labor, the capitalist of the manufacturing sector can expand without necessarily increase. As a result, the capitalists can charge a price above the fixed wage rate, and then reinvest the profit into fixed capital and enables this sector to expand more. At the final stage, the country will eventually shift from traditional economy into modern economy. This universal model combines an analysis of the historical experience of Japan and Western European countries with the central ideas of the classical economists to explain development

process. Moreover, this model emphasizes income per capita as the measurement of economic success.[153]

Other common models during those years, whether it was Raul Prebisch's 'center vs. periphery' (1949) or Harvey Leibenstein's 'big push' (1957) or W. W. Rostow's 'stages of economic growth' (1960), had also suggested a linear and gradual model of social change. Those models argued that the informal and subsistence economy of all developing countries would be transformed into a modern economy regardless of their differences in size, history, culture, endowment, etc.[154]

Contrary to this optimism, many research projects conducted in the 1970s had shown the persistence of the informal sector especially within rural areas. British anthropologist, Keith Hart stated that despite the external pressure from the capitalist economy, most of rural migrant workers in Accra, Ghana were still engaged in informal activities.[155] This pioneering study was confirmed later on by similar study by ILO World Employment Commission, which was conducted in Kenya in 1972. Moreover, this study concluded that the informal sector was not only persisted but it was expanded to include profitable and efficient enterprises as well as marginal activities.[156] It means that rather than simply a low-income and backward economic activity, the informal sector is considered by these studies as creative, efficient and resilient activities. Therefore, some experts found that the term 'informal' is misleading. Robert Neuwirth prefers to use the term of System D, which comes from French word *débrouillard*. This word literally means resourceful and ingenious. System D is used to define the inventive, self-reliance, and the do-it-yourself economy that exist by not being regulated by the government, and for most part, without paying taxes. Not only that, this sector is also growing around the world including within

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[153] W. Arthur Lewis, "Economic Development with Unlimited Supplies of Labour," *the Manchester School* 22 (1954).

[154] Paul E. Bangasser, "The ILO and the informal sector: an institutional history", *Employment Paper 2000/9,* International Labour Organization (ILO), 2000. Paul E. Bangasser, "The Ilo and the Informal Sector: An Institutional History," *Employment Paper* 9 (2000).

[155] Keith Hart, "Informal Income Opportunities and Urban Employment in Ghana." *The Journal of Modern African Studies* 11, no. 1 (1973): 61-89. http://www.jstor.org/stable/159873.Kevin Hart, "Informal Income Opportunities and Urban Employment in Ghana," *The Journal of Modern African Studies* 11, no. 1 (1973).

[156] ILO Report, "Employment, incomes and equality: a strategy for increasing productive employment in Kenya," *An Interagency Report supported by UNDP & ILO,* 1972. ILO, *Employment, Incomes and Equality: A Strategy for Increasing Productive Employment in Kenya* (1972).

developed economies. According to Neuwirth, "Estimates are that the informal economy around the world is [worth] about $10 trillion a year and if it is combined into a one country, it would be the second-largest economy on Earth, rivaling the United States economy."[157]

ILO defines informal sector as "a sector may be broadly characterized as consisting of units engaged in the production of goods or services with the primary objective of generating employment and incomes to the persons concerned. These units typically operate at a low level of organization, with little or no division between labor and capital as factors of production and on a small scale. Labor relations - where they exist - are based mostly on casual employment, kinship or personal and social relations rather than contractual arrangements with formal guarantees."[158] Furthermore, informal sector activities are largely ignored, rarely supported, often regulated and sometimes actively discouraged by the Government.

That definition suggests that informal does not indicate a location of the activities such as rural or the periphery of the cities. It also does not limit the meaning to certain economic jobs or economic activities. Informal is the way of doing things, characterized by:

(a) ease of entry;
(b) reliance on indigenous resources;
(c) family ownership of enterprises;
(d) small scale of operation;
(e) labor-intensive and adapted technology;
(f) skills acquired outside the formal school system; and
(g) unregulated and competitive markets.[159]

There are many debates related to the emergence of the informal economy. One is questioning its impact whether this sector brings benefit to the system as a whole. Some see it as a pathology that need to be cured, but others regard it as an alternative that makes the economy continues to grow and stabilize. The first group considers informal economy represents unprotected workers, excessive regulation, low productivity, and unfair competition, evasion of the rule of law, underpayment or nonpayment of taxes, and work "underground" or in the

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[157] Robert Neuwirth, *Stealth of Nations: The Global Rise of the Informal Economy* (New York: Pantheon Books, 2011).
[158] Paul E. Bangasser, "The ILO and the informal sector: an institutional history" ...page 46.
[159] ILO Report. page *6.*

shadows. Many believe that informal enterprises should be brought under the formal regulatory environment to increase the country's tax base and reduce the unfair competition to formal businesses. The second group considers diversification as a good thing. It helps individuals and society becoming more resilient toward shocks.

There are also scholars who are focusing on the issue of its relationship with the formal economy. The Dualist as presented by the Lewis model argues that both sectors operate separately or with a very few linkages. In this situation, the informal sector comprises the less advantage sector. Contrary to the Dualist, many experts argue on the interconnectedness of these two sectors. *The Structuralists* see the informal and formal are intrinsically linked where Capitalists subordinate workers from both sectors in order to keep the price of goods and services low.[160] These questions are important in defining the direction of the current research on the informal economy.

In 2007, the Latin America Division of the World Bank published Informality: Exit and Exclusion, a book co-authored by Guillermo Perry, William F. Maloney, Omar Arias, Pablo Fajnzylber, and Jaime Saavedra. The co-authors proposed a holistic model of the composition and causes of the emergence of the informal economy or informality. Regarding the causes or drives informality, they specified three different forms of both Exit (voluntary informality) and three different forms of Exclusion (involuntary informality). The term 'exit' is appropriate for the individuals or enterprises that used to be in the formal sector then move to informal, while 'exclusion' is for the ones who never been formal. The scholars believe there is no single factor that is able to explain it comprehensively, and most of the cases are considered as result of a mix interaction between voluntary and involuntary informality.[161]

The three forms of Exit are opportunistic evasion, defensive evasion, passive evasion or state irrelevance. Opportunistic evasion is informality that is caused by motives of evading tax and labor codes or law and conducting illegal activities. The informality is considered as defensive evasion when the informal workers and entrepreneurs move to informal activity in response to burdensome, captured, and weak state. For instance, the conflict in Iraq had weakened the state

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[160] Martha Alter Chen, "The Informal Economy: Definitions, Theories and Policies," *WIEGO Working Paper No.1* (August 2012), http://www.wiego.org/sites/wiego.org/files/publications/files/Chen_WIEGO_WP1.pdf ; ibid.
[161] Ibid*.,* page 9-11.

in providing the livelihood for Iraqis. Governmental job had been the main sources for Iraqis to get income for the past years, thus when the Government collapsed, they turned to the informal economy to earn a living.[162] Other instance is how global economic crises makes people in Johannesburg to work informally by selling at the city street.[163] Lastly, the passive evasion is a voluntary informality, which is caused more by the prevailing pre-modern institutions such as Bazaar economy or a non-state institution such as traditions within the localities.

Different from the previous ones, the informality happens involuntarily mostly due to structural reasons. For instance, worker cannot get formal jobs due to labor market segmentation. A study on informal childcare work concludes that migrant workers stay in informality because when it is formalized, it will become too expensive. There is no incentive for the family (or the mother) to use the informal childcare services because it cost more than they earn.[164] The economic activities inside refugee camps are also kept informal due to the nature of the legality of the camp itself. Informal economy has become the lifeblood of the camp, but at the same time, it also has made the non-permanent settlement ‘permanent’.[165] Another reason for Exclusion is burdensome in entry regulations or excessive taxing which prevents firms from formalizing. Many informal health care practices such as herbal medicine or faith healers are maintaining their activities within informal framework because of the regulations. Many of these practices are still exist in many parts of the world.[166]

Informality also exists in insurance. A study from the World Bank notices the persistence of informal insurance in many households in low-income countries. The examples include drawing down savings, engaging in a reciprocal gift exchange, selling physical assets, and diversifying income-generating activities. Those are not arranged through a legally binding

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[162] Robert Looney, "Economic Consequences of Conflict: The Rise of Iraq's Informal Economy," *Journal of Economic Issues* 40, no. 4 (2006).
[163] Jennifer Cohen, "How the Global Economic Crisis Reaches Marginalised Workers: The Case of Street Traders in Johannesburg, South Africa," *Gender and Development* 18, no. 2 (2010).
[164] Mary Tuominen, "The Hidden Organization of Labor: Gender, Race/Ethnicity and Childcare Work in the Formal and Informal Economy," *Sociological Perspectives* 37, no. 2 (1994).
[165] Rahul Oka, "Unlikely Cities in the Desert: The Informal Economy as Causal Agent for Permanent 'Urban' Sustainability in Kakuma Refugee Camp, Kenya," *Urban Anthropology and Studies of Cultural Systems and World Economic Development* 40, no. 3/4 (2011).
[166] Kate Hampshire et al., "Informal M-Health: How Are Young People Using Mobile Phones to Bridge Healthcare Gaps in Sub-Saharan Africa?," *Social Science & Medicine* 142 (2015).

contract or state bureaucracy. The mutual help is ensured through the existence of social norms and trust. Everybody helps with the expectation to receive similar help in the future. This arrangement is often very effective in the right circumstances, but it is hardly able to cope with large-scale economic shock or huge natural disasters.[167]

Altogether, these theories of informality help us to understand the reasons why people in majority Muslim countries maintain their traditional risk management (as we will see in the case of Pakistan), instead of using the modern, formal, Sharia-compliant of Islamic insurance. Furthermore, the sophisticated approaches on informality of the recent literature enable us to consider traditional risk management not as pathology or backwardness, but a sign of resourcefulness and ingenuity.

Social capital

This next group of literature on social capital proposes a parallel explanation of the phenomenon of the lack of Islamic insurance development. It comes naturally on the list after the discussion on the informal economy. It suggests that a society with rich social capital will have more capability to develop alternative mechanisms. The informal insurance services use social capital as the basis of their activities. Even for the formal one such as mutual or cooperative insurance, it still depends also on the existence of trust between its members. As most individuals could not deal with an economic loss only by themselves, the solution would be to develop a mechanism of risk sharing through mutual insurance. This effectiveness of this mechanism depends on the extent of the availability of social capital within the community.

Social capital has been an essential part of Sociology for a long time. Emile Durkheim did not use the term on his discussion on *Suicide* (1897), but he referred it conceptually when he talked about how individual's connection to society can protect the individual from anomie and self-destruction. Durkheim explores the differing suicide rates among Protestants and Catholics,

[167] Jonathan Murdoch, *Between the Market and State: Can Informal Insurance Patch Safety Net?*, *Stiglitz Summer Research Workshop on Poverty* (Washington: 1999).

arguing that stronger social control among Catholics results in lower suicide rates.[168] The other French writer, Alexis de Tocqueville, also highlighted the importance of social participation within the American society as he observed during his visit there in the early 19th century. According to him, Americans were prone to discuss public matters collectively. The social participation of the people along with a high level of transparency were the reasons for American democracy to work.[169]

The next scholar on social capital would be Pierre Bourdieu. Bourdieu can be considered as the pioneer for the recent study of social capital. He identified the value of social capital, which he defined as “the sum of the resources, actual or virtual, that accrue to an individual or a group by virtue of possessing a durable network of more or less institutionalized relationships of mutual acquaintance and recognition.” [170]As a neo-Marxist, he examined the role of different types of capital including social capital in the reproduction of power relations within society.

Furthermore, James Coleman developed Bourdieu differentiation of capitals and provided a clearer theoretical framework on social capital. According to him, social capital has a similar function as other capitals: physical, financial, and human capital, which provides structure for facilitation human actions. Social capital can take three forms; firstly, obligations and expectations which depend on the trustworthiness of the social environment, secondly the capacity of information to flow through the social structure in order to provide a basis for action and thirdly the presence of norms accompanied by effective sanctions. In his discussion on obligations and expectations, he describes the situation of doing favors for someone as "credit slips." Should an individual need a favor, he is essentially giving someone else a credit slip, which signifies that he will be paid back for his goods and/or services. He mentioned how the strong ties among members of the Orthodox Jewish community in Brooklyn enable them to trust each

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[168] Pickering, W.S.F.; Walford, Geoffrey (2000). *Durkheim's Suicide: A Century of Research and Debate*. Routledge. ISBN 978-0415205825. W.S.F. Pickering and Geoffrey Walford, *Durkheim's Suicide: A Century of Research and Debate* (Routledge, 2000).

[169] Tocqueville, *Democracy in America* (Harvey Mansfield and Delba Winthrop, trans., ed.; Chicago: University of Chicago Press, 2000) Tocqueville, *Democracy in America* (Chicago: University Chicago Press, 2000).

[170] Pierre Bourdieu, (1986) “The Forms of Capital in Baron”, S. Field, J. Schuller, T. (eds.) (2000) S*ocial Capital - Critical Perspectives.* Oxford University Press Pierre Bourdieu, *The Forms of Capital in Baron* (Oxforld University Press, 1986).

other then make trade transaction easier. [171] The existence of social capital can be measured from the level of trustworthiness, which enables that process to happen.

Robert Putnam completed the conceptualization of social capital. His works have expanded the discussion of social capital beyond academic circle to a wider public, but more importantly, he strengthened the conceptualization of social capital as an attribute of communities rather than individual. Putnam started his research on social capital by studying the local governments in Italy. In *Making Democracy Work: Traditions in Modern Italy,* Putnam wrote that northern Italy's history of community, guilds, clubs, and choral societies led to greater civic involvement and greater economic prosperity. Similar with Tocqueville's finding on the American society, the 'networks and norms of civic engagement' allows to build trust. Therefore, trade and democracy flourish in this locality. Meanwhile, the agrarian society of Southern Italy is less prosperous economically and democratically because of less social capital.[172]

Similarly, Francis Fukuyama compared the relative economic performance of different nations and cultures based on differing levels of trust. He underlines the interconnectedness of economy to the cultural life of society. He believes that nation cultures contain underlying principles that foster social and economic prosperity. It is a certain set of informal values or norms shared among the members of a group, which permit cooperation among them. In his book, *Trust: The Social Virtues and The Creation of Prosperity,* he concluded that society with high level of social trust will be able to create the flexible, large-scale business organizations that are needed to compete in the new global economy.[173] Coleman, Putnam, and Fukuyama agreed that trust as the main feature of social capital.

At later development, social capital had started to gain attention in the economics discourse too. This importance of social capital in economic development has captured the attention of many international development agencies such as the World Bank and OECD. Not only focusing on technical assistance, these organizations has been adjusting its strategy to

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[171] James Coleman, "Social Capital in the Creation of Human Capital," *American Journal of Sociology* 94, no. Supplement S95-S120 (1988).

[172] Robert Putnam, *Making Democracy Work: Civic Traditions in Modern Italy* (Princeton, New Jersey: Princeton University Press, 1994).

[173] Francis Fukuyama, *Trust: The Social Virtues and the Creation of Prosperity* (Free Press, 1995).

include the development of the social fabric of the society: the institutions, relationships, and norms that shape the quality and quantity of a society's social interactions.[174] Regarding insurance, many of these agencies have tried to find alternative ways to provide healthcare to low income communities. Many of these new alternatives or unknown policy for instance Community-Based Health Care need to be supported by a cohesive community. They believe that a community with a high level of social capital will be more inclined to go through change.[175]

Beyond the component of trust, Putnam provides a more comprehensive definition on social capital by adding other crucial components. He defines social capital as 'trust, norms, and networks that can improve the efficiency of society by facilitating coordinated actions'.[176] This definition involves three aspects of social capital: trustworthiness (how people anticipate that others will behave in the future), norms (the informal laws that govern exchanges and daily life), networks (the connections between individuals). According to Putnam, these three aspects can be observed through the level of increase/decrease level of membership of professional, political, or religious organizations and informal socializing.

The recent scholars have enriched Putnam's basic definition resulting a more sophisticated understanding on social capital. Some of them have tried to improve Putnam's methodological approach by focusing on the changing pattern of membership rather than simply its number. Others are focusing more on the term 'social' rather capital meaning that they approach the concept not as properties of individual or collective that can be identified independently but more social properties that can only be accessed through ties in the network. Putnam focuses on 'wires' where information and resources run, hence the network and relationship are its core component, but others focus more on 'electricity' or information and resources that running through the wires.[177]

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[174] S. Cote and T. Healy, *The Well-Being of Nations: The Role of Human and Social Capital* (Paris: Organization for Economic Co-operation and Development, 2001).

[175] Hermann Pierre Pythagore Donfouet and Pierre-Alexandre Mahieu, "Community-Based Health Insurance and Social Capital: A Review," *Health Economics Review* (2012).

[176] Putnam, *Making Democracy Works. Page* 167.

[177] Daniel P Aldrich, *Building Resilience: Social Capital in Post-Disaster Recovery*. Chicago: University of Chicago Press, 2012. Page 30 Daniel P Aldrich, *Building Resilience: Social Capital in Post-Disaster Recovery* (Chicago: University Chicago Press, 2012).

The recent scholarship on social capital acknowledges that social capital is not panacea for social problem. Social capital is not necessarily to be societal goods. The reason is social capital works in certain circle or social connection. For instance, Fukuyama asserts that trust does not work equally across society. He refers to a "radius of trust" which means a circle of people among whom cooperative norms operate. In some societies, a narrow radius of trust produces a two-tier moral system, with good behavior reserved for family and personal friends, and a lower standard of behavior in the public sphere. This explains the practice of nepotism and corruption in many countries.[178]

This differences on how it works has led to a further study on the differentiation of social capital. As networks, social capital can be categorized into three types of connections: bonding, bridging, and linking. Bonding (exclusive) social capital refers to relations amongst relatively homogenous groups such as family members and close friends and is similar to the notion of strong ties. Putnam mentions the examples of bonding social capital as being ethnic fraternal organizations and church-based women's reading group. This form of network centers on horizontal ties between individuals who are quite similar to each other and may live the same area. This type of network can produce negative externalities as documented by Daniel Aldrich in his study on post-disaster recovery. He acknowledges that social capital has more role compares to financial assistance in the recovery process, but it also has a downside.

Aldrich provides a thorough empirical study of how a strong bonding hampered the recovery process for instance in the case of Hurricane Katrina, 2005. FEMA had trouble to locate temporary housing/trailers in the area with strong political participation. The local citizens successfully opposed the existence of FEMA trailers in their area. Moreover, strong sense of belonging to a group can create indifference or even hostility to non-members.[179] Bridging (inclusive) social capital refers to relations with distant friends, associates and colleagues. It refers to the horizontal network to extra local, crossing ethnic, racial, and religious cleavage, for instance civil rights movements and ecumenical religious organizations. Linking social capital refers to vertical relations between individuals and groups in different social strata in a hierarchy

[178] Francis Fukuyama, *Social Capital and Civil Society* (International Monetary Fund, 2000).
[179] Daniel P Aldrich, *Building Resilience: Social Capital in Post-Disaster Recovery*, Page 32.

where different groups access power, social status and wealth. This to include the capacity to leverage resources, ideas and information from formal institutions beyond the community.

Understanding how the networks work can help us to understand informal insurance. Aldrich notes that in disaster recovery, social ties can serve as informal insurance, by providing information, financial help, and physical assistance as alternative of market-based insurance.[180] Some scholars even argued, "Being embedded in a network of higher kin composition, greater density, larger size, and lower diversity increased the probability that a respondent received recovery support".[181] In other words, the higher the bonding is, the most likely that people rely more on informal and community based insurance mechanisms.

Overall, this section shows the significance of social capital, understood as trust, norms and networks in examining the emergence of alternative insurance. Furthermore, the literature on social capital pushes us to ask the question of economic security beyond framework of economy. The argument for modern insurance company is the need to have a financially capable entity to handle economic insecurity. The risks are simply too difficult and too expensive to be handled by a single individual. To the contrary, social capital provides us with a different approach on the problem. As many studies on post-disaster recovery show that, the financial capability has less role in community recovery. The difference between resilience and disrepair lies in the depth of communities' social capital. Likewise, those communities rely more on alternative risk managements due to the existence of robust social networks which help them in providing better economic security.

Summary: from static comparisons to a dynamic conception of the 'political life' and the 'social life' of Islamic insurance

In considering the central question of why Islamic insurance systems develop well in some countries, but not in others, this chapter provides various possible theories to answer it. The literature on Islamic insurance up to this date have provided us with a wealth of insight and

[180] *Ibid, 45.*
[181] John J. Beggs, Valerie A. Haines, and Jeanne S. Hurlbert, "Situational Contingencies Surrounding the Receipt of Informal Support," *Soc Forces* 75, no. 1 (1996).

information. However, almost all of them treat Islamic insurance as an autonomous and static entity. In fact, Islamic insurance is part of a complex economy that is embedded in the country's particular social institutions. Moreover, evolutionary process and institutions in each country have significant roles in shaping their population economic behavior, which is mostly neglected in many studies of Islamic insurance. This dissertation offers a new as a means of adding breadth and depth to existing studies of Islamic insurance implementation.

By using the various theories mentioned previously in this chapter, this dissertation offers a qualitative research on the 'political life' and the 'social life' of Islamic insurance in Indonesia, Malaysia, and Pakistan. The development gap between these countries on Islamic insurance rests on the analysis of Islamic insurance as a product of political decision and social practice. It explores Islamic insurance development gap as part of a broader socio-cultural development and to consider economy as an evolving entity of bounded rationality. In other words, our theory focuses on how the decision of political actors to embrace and regulate Islamic insurance as a state's policy and the acceptance of public of Islamic insurance in their daily lives influence the development of Islamic insurance in these countries.

The term 'political life of Islamic insurance' is developed based on the argument that Islamic insurance arrangements are not a passive response to some efficiency criterion but rather the product of political deals within country's polity that determine which laws are passed.[182] The payment, involving all the details of how providers are paid, incentives, and so on; and organization, the structure of Islamic insurance system, risk pooling and the division of labor of institutions within it are an outcome of political decisions. The constitution, political pattern, and institutional arrangement provide a 'path dependence' for each country in operationalizing the Islamic reform. In the upcoming chapters, the political life of Islamic insurance in these three countries is examined as a result of complex bargains made between various groups within each country polity, and those bargains are structured by the country's fundamental political institutions.

The usage of the term 'social life of Islamic insurance' refers to a framework for understanding Islamic insurance as a commodity whose worth lies both within and beyond its

[182]Calomiris, *Fragile by Design the Political Origins of Banking Crises and Scarce Credit*.

exchange value.[183] It calls attention to how insurance moves between registers of value among different stakeholders and at various scales of analysis. It also encompasses how meaning ascribed to insurance changes over time. It is the behavior, the habit, and action of the consumers and providers within the system. The concepts of risk, risk sharing, distributive justice, generalized reciprocity, and hedging against financial catastrophe are understood and addressed in relation to the values, social capital, and culture in local worlds. In fact, different stakeholders have presented insurance as both a concept and an institution to the public in various ways. Public perceptions of and demand for insurance are not static. They are sensitive to changing policy, practice, experience, and flows of information.[184] According to Amy Dao and Mark Nichter, we can analyze the social life of Islamic insurance through the interaction of various sociocultural, economic, political, historical, and global and local that contribute to the "careers" of Islamic insurance plans in these countries.[185]

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[183] Arjun Appadurai, *The Social Life of Things Commodities in Cultural Perspective* (Cambridge [Cambridgeshire] ; New York: Cambridge University Press, 1986).
[184] Amy Dao and Jessica Mulligan, "Toward an Anthropology of Insurance and Health Reform: An Introduction to the Special Issue," *Medical Anthropology Quarterly* 30, no. 1 (2016): 5–17.
[185] Amy Dao and Mark Nichter, "The Social Life of Health Insurance in Low- to Middle-Income Countries: An Anthropological Research Agenda," *Medical Anthropology Quarterly* 30, no. 1 (2016 2016).

CHAPTER III

MALAYSIA

Since the enactment of the Takaful Act 1984, Malaysia's Islamic insurance industry continues to demonstrate a positive growth rate. It becomes a significant contributor to Malaysia's overall Islamic financial system. In 2015, Malaysia had the largest Islamic insurance market in South East Asia with a 62% market share and the largest Family Takaful market globally. There were eight composite companies (i.e., selling both Family and General Takaful business) and three pure Family Takaful operators in Malaysia. In the same year, the market share of the Islamic insurance industry in Malaysia was 12% of the total conventional insurance. Malaysia is also considered as the leader in Islamic insurance regulations. Malaysia is the first country in the world to implement a risk-based capital (RBC) framework for Islamic insurance. This novel framework requires Islamic insurance companies to be more transparent by disclosing its agency fees in its sales.[186]

Islamic insurance of Malaysia develops within a dual banking and financial system. The Islamic financial system coexists with the conventional financial system. The Islamization in Malaysia was not presented as an aspiration of replacing the existing political economy structure of the country. The Islamic financial system is regarded as a supplement to the existing system. Malaysia is considered as the first country to implement this dual system. Many Muslim majority countries recognize Malaysia's Islamic finance as the model to emulate.

This chapter discusses the development of Islamic insurance in Malaysia. It begins with a brief introduction of Malaysia as a multi-ethnic Islamist state. This section stresses the status and role of Islam in the state building, the ethnic-based politics, the economic structure, and the political actors of Islamic politics of Malaysia. Also, this introduction explains the structural and cultural environments of Malaysia where Islamic insurance develops. After this brief

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[186] Farzana Ismail et al., "Global Takaful Report 2017: Market Trends in Family and General Takaful," Milliman Research Report (Milliman, July 2017), http://www.milliman.com/uploadedFiles/insight/2017/Takaful-2017-full-report.pdf.

introduction, this dissertation continues with a section on Islamic insurance development in Malaysia. It provides detail information on the fact and figures of Islamic insurance in Malaysia, and more importantly the characteristics of Islamic insurance as a political product and social practice within Malaysian polity and society. We can consider this section as the dependent variable of this dissertation. The next two sections explain this development through the independent variables of 'political life' and 'social life' of Islamic insurance in Malaysia. The first independent variable explores the catalysts and the political coalitions behind Islamic insurance during the Mahathir (1981-2003) and the post-Mahathir regimes. The second independent variable relates to Malay's social transformation, which is responsible for the development of the 'modern' redefinitions of Islamic economic beliefs that have shaped the Malay understanding of entrepreneurship, human agency, Islamic duty, and financial obligation.[187] This modern understanding of 'Islam' is influential in how Islamic insurance has been presented to the public.

The structure of a multi-ethnic Islamist State

Malaysia is a federal constitutional monarchy consists of thirteen states and three federal territories. Although Islam is the official religion of the country, Malaysia is not a state where the law is ultimately derived from Islam. Ethnicity is important in Malaysia's politics. A coalition government dominated by Malay Muslims has ruled Malaysia since its independence in 1957. Malaysia can also be described as an illiberal democracy. The country has procedures and institutions characteristic of democracy, such as regular elections, minority rights and free press. However, the government maintains control and intervenes in most aspect of social life of its citizens.[188]

The British colonialism had a prominent role in shaping the political and economic structures of Malaysia. This prominent role includes influencing the religious life and the relationship between Malay states and Muslim communities. The British consolidated the apparatus of centralized government and Malaya's capitalist economy for almost 100 years of

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[187] Patricia Sloane-White, *Corporate Islam [E-Book] Sharia and the Modern Workplace* (2017).

[188] Meredith L. Weiss, *Protest and Possibilities: Civil Society Amd Coalitions for Political Change in Malaysia* (Stanford University Press, 2005).

colonial rule in the Malay Peninsula and the Northern Borneo. After a brief period of Japanese occupation during World War II, the British Military Administration returned to Malaya and proposed the formation of a newly independent country. The decision of giving independence was due to the lack of financial resources and popular support to maintain the British' colonies in the post WW II. However, the proposal clearly showed British's intention in ensuring their economic interests would be safeguarded after independence.[189] Therefore, rather than breaking up with the colonial past, the formation of independent Malaysia in 1957 was designed to inherit the colonial political, legal, and economic system.

Later, the Islamic dimension was added in the overall system since the 1980s. The inauguration of Mahathir Mohamad as Malaysia's Prime Minister in 1981 set Malaysia gradually 'as the fruit of a happy union between strict Islam and modern capitalism'.[190] That concept shows Malaysia's ambition to be the Islamic financial hub of the Southeast Asian region and the world, but at the same time, it wants to maintain the religious conservatism in the social life. The following discussion provides a brief introduction of Malaysia as a state, particularly in its relation to the role of Islam in state building, its multi-ethnic/religious circumstances, its capitalistic economy structure, and its essential political actors.

Malay nationalism

Historically, Malaysia has its origins in the Malay Kingdoms present in the area, which, from the 18th century, became subject to the British Empire. Based on the latest United Nations estimation, the population of Malaysia in 2019 is around 32 million or equivalent to 0.42% of the total world population.[191] The territory of this federal constitutional monarchy is separated by the South China Sea into two similarly sized size regions, Peninsular Malaysia and Malaysian Borneo. The Peninsular Malaysia also known as Malaya or West Malaysia, which contains the capital city of Kuala Lumpur, accounts for the majority (roughly 92%) of Malaysia's population

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[189] Ira M. Lapidus, *A History of Islamic Societies*, 2nd ed.. (Cambridge New York: Cambridge New York : Cambridge University Press, 2002).
[190] Weiss.
[191] Department of Economic and Social Affairs Worldometers, Population Division, *World Population Prospects: The 2017 Revision* (Worldometers, 2017).

and economy. Malaysian Borneo or East Malaysia is less populated and overall less developed in its settlements than its West. However, East Malaysia's land mass is larger, and it has more of many natural resources including oil and gas reserves.

As mentioned earlier, the independent Malaysia was not a result of a nationalist opposition against the British rule, but it was a formation of an independent Malay state governed by its traditional elites with a full support from the former ruler of the colony. In 1946, upon the return of the British to Peninsula Malaya after Japanese occupation, the British Military Administration proposed for the creation of the Malayan Union, which consists of the federated and un-federated Malay states, Singapore, Malacca, and Penang. According to this proposal, there would be a central government for the whole region where Malay, immigrant Chinese and Indian communities have equal access to political power.

This initial proposal was in fact bypassing the traditional authority of the Sultanates. The Malay nationalists strongly opposed this proposal and successfully pressured the British to replace the Malayan Union with the Federation of Malaya in 1948. The modified proposal of the Federation of Malaya preserved the separate existence of the several Malay states and guaranteed the supremacy of Malay interests.[192] The Malayan Communist Party, which primarily supported by Chinese workers, was the only one who opposed the formation of the Federation. The Malayan Communist Party, who had organized anti-Japanese resistance in the 1940s, condemned the Federation as a reunion of "British imperialism and Malay feudalism". [193]

At the same time, the Malay elite knew that the British would not grant independence unless the Malays could convincingly demonstrate that they could work with the immigrant Chinese and Indian communities. In order to convince the British, the Malay elite initiated the formation of an inter-ethnic political coalition called the Alliance in 1954 comprising the United Malays National Organization (UMNO), the Malayan Chinese Association (MCA), and the Malayan Indian Congress (MIC). The Malay elite gained more confidence after their landslide victory in the first elections for the legislature in 1955. This victory showed that the Malay elite could lead a

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[192] Lapidus. page 677.

[193] Jaclyn Ling-Chien Neo, "Malay Nationalism, Islamic Supremacy and the Constitutional Bargain in the Multi-Ethnic Composition of Malaysia," *International Journal on Minority and Group Rights* 13, no. 1 (2006), http://dx.doi.org/10.1163/157181106777069950. citing Parmer…

culturally and religiously diverse nation. Moreover, the coalition and its electoral triumph had shown the overwhelming political support among the masses upon the idea of power-sharing governance of this new federation.

In 1957, an independent Malayan state was officially formed with the support of Malay officials, Chinese merchants, and Indian intellectuals under the leadership of Tunku Abdul Rahman. Under the new constitution, the dominance of Malays or *Bumiputera* in education, job, the state bureaucracy, and reservation of land and of non-Malays in the economy were established. The Federal Constitution declares Islam as the official religion of Malaya, but it also guaranteed freedom of worship for other religious communities. Article 52 of the Constitution stated that Malay language (*Bahasa Melayu)* as the official language of the Federation. Bahasa Melayu would soon replace English, Chinese, and Tamil in state schools. In 1993 the Federation of Malaya was reorganized to include North Borneo and Singapore (though Singapore withdrew in 1965), and the extended federation was officially renamed Malaysia.

Ethnicity is the backbone of Malaysian politics. Malaysia's population is just over 50 percent ethnic Malay, with Chinese Malaysians composing 22.7 percent, Indian Malaysian making almost 7 percent, and non-Malay Bumiputera and other Indigenous groups another 11.8 percent.[194] The law defines Bumiputera as consists of Malays and non-Malays indigenous communities. It includes Malays, Thais, Eurasian, hill peoples in the Malay Peninsula (known as *orang asli*), and indigenous Borneans (i.e. Dayak, Kadazandusun, and many others) but excludes Malaysian of Chinese and Indian descent. Article 160 of the Constitution only states the criteria for a person to be considered a Malay; which is to profess the religion of Islam, habitually speak Malay language, conform to Malay custom and be born to a Malaysian parent.[195]

In the mid-year of 2017, the Department of Statistics Malaysia estimated the country's population as slightly over 32 million citizens and non-citizens. The 28.7 million citizens consisted of the Malays and non-Malay indigenous groups that reside in Malaysian Borneo (*Bumiputera*) at 19.78 million and the Chinese at 6.66 million and Indians just below 2 million. Chinese

[194] World Atlas, "Ethnic Groups of Malaysia," *Society* (accessed 16 January 2018, https://www.worldatlas.com/articles/ethnic-groups-of-malaysia.html.

[195] malaymail.com, "Bumiputera: Are You One? Or Can You 'Become' One in Malaysia?," July 26, 2017, https://www.malaymail.com/s/1429005/bumiputera-are-you-one-or-can-you-become-one-in-malaysia#Hj6u5yUBytSWCDwQ.99.

Malaysians include both long-settled *Peranakan* or Chinese descents and the larger group of immigrants that arrived in the 1800s and early 1900s, which can be divided still further among different provincial or dialect groups. The Indian community, though mostly Tamil, contains significant numbers of Telugu and Malayalam speakers in addition to Punjabi, Sikh, and Indian Muslim minorities.[196]

The non-Malay communities have been vital for the economy of the country. Chinese and Indian labor skill was crucial to the tin mining and rubber industries, respectively, which were the two principal revenue earners for the country during the colonial era. The vital significance of these communities was one of the reasons why the British colonial regime included them as citizens in the British's initial proposals of the formation of the Federation. Chinese and Indian labor skill was important for maintaining the British' economic interest in the post-colonial era of Malaysia. Moreover, both the British and the Malay elite did not want the immigrant Chinese to support the Communist cause to break the colonial economic structure of the country.

The Federal Constitution does not necessarily exclude the non-Malay from the political domain. There have been some of the prominent non-Malay legislators at both federal and state levels. Non-Malay can achieve senior public service positions, such as ambassadors and counselors in mission abroad. The Malaysian judicial service boasts of an array of non-Malay judges. However, there is political power imbalance between the Malay and non-Malay communities. Non-Malay has no reasonable representation in the federal cabinet, the parliament, the various state executive councils, and state assembly.[197] The prime minister and deputy prime minister have always been Malays, though there is no constitutional provision restricting others. The Malay also dominates the civil service and the armed forces. As agreed, since independence, the political system of having a Malay core is preserved to maintain the historical character of Malaysian society. This dominance has continuously supported by government policies that usually give preference to Malay Bumiputera over other groups.

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[196] CIA World Factbook, "Malaysia Demographics Profile 2018," accessed April 30, 2018, https://www.indexmundi.com/malaysia/demographics_profile.html.
[197] Chandra Muzaffar, "Power Sharing: The Significance of the Malaysian Experience for Muslims in Multi-Religious Society," *Middle East Affairs Journal* 4, no. 1-2 Winter/Spring (1998).

Malaysia was relatively successful in operating a system of *consociational* democracy based on multi-ethnic elite bargaining until the breakdown of the Alliance due to the ethnic riot of May 1969. Since 1971, Malaysian political system cannot be considered as consociational. Malaysia under the leadership of Mahathir Mohamad of the UMNO has been transformed into a Malay authoritarian government where the Malaysian regime has promoted institutions and policies that favor more Malays (who are also Muslim) at the expense of non-Malays (Chinese Malaysian, India-Malaysian). There were regular elections and a parliament, but these democratic institutions did not make government turnover possible, instead of lending the regime legitimacy and encouraging some political responsive.[198] However, the UMNO under Mahathir was more responsive toward constituent interests than Indonesia's Golkar Party was under Soeharto. Soeharto's New Order regime was far more repressive than Mahathir's Malaysia.

The Malaysian regime since the early 1970s has relied on two groups, each of which receives benefits from the regime in exchange for political support. The regime relies on the explicit system of Malay favoritism targeting ordinary Malays and rewarding wealthy Malay cronies. The favoritism was actualized through the implementation of the New Economic Policy (NEP), an affirmative government policy to improve the economic wellbeing of the Malays. In fact, the wealthy Malay elites were the result of this affirmative policy. In sum, the actual Malaysian political system under Mahathir rests on an explicit cross-class alliance between the Malay masses and a group of wealthy Malay elites with extensive involvement in both the corporate world and politics.[199]

The Chinese Malaysian minority is economically dominant but have mostly been left out of the ruling coalition. Moreover, the Chinese Malaysia had not been able to create a strong communal-wide organization. The new wealthy Malays and Chinese Malaysian entrepreneurs are the corporate business sector in Malaysia. Both favor a more liberal legal regime that facilitates business activities. The difference is that the wealthy Malays have the capital

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[198] Tom Pepinksy, *Economic Crises and the Breakdown of Authoritarian Regimes : Indonesia and Malaysia in Comparative Perspective* (New York: Cambridge University Press, 2009).
[199] Thomas B. Pepinsky, "Capital Mobility and Coalitional Politics: Authoritarian Regimes and Economic Adjustment in Southeast Asia," *World Politics* 60, no. 3 (2008).

investment that is fixed in Malaysia, while Chinese Malaysian have mobile capital. According to Pepinsky, this is the reason Mahathir relied on policies of capital controls and an exchange rate peg in dealing with the 1997 Asian Financial Crisis. Malaysia implementation of these policies reflects the Mahathir regime's dependence on an alliance between Malay fixed capital and Malay labor.[200]

Islamic supremacy

Islamic matters were under the control of the state level administrators, and not the federal government. The British set out a special place for Islam in their administration of the Federated Malay States, granting the sultans, or the traditional rulers, authority and status, but only in limited matters concerning religious practice, ritual, and the laws of Muslim personhood, family life, and marriage (*munakahat*). Sharia courts adjudicate matters concerning Sharia matters in the individual state-based jurisdictions. The single exception to that legacy is *muamalat*, the regulation of Islamic finance, which, since its inception in Malaysia in 1983, has been governed by federal law.[201]

Despite its centralized politico-administrative system, Malaysia is an agro-urban society with a differentiated social formation. Malaysia has an institutional configuration that recognizes the division between state and religious spheres.[202] The Federal government represents the state sphere and the Sultan and State level religious institutions represent the religious sphere. Throughout the Malay Peninsula, administration of religious affairs and the creation of chief *qadies*, councils, and Sharia committee brought Islamic legal, educational, ritual, and financial affairs under the control of the Sultan, assisted by state level religious agencies, the *Majilis Agama Islam* (Council of Islamic Religion and Religious Council) and the Department of Religions Affairs (or Religious Department).

[200] Ibid.
[201] Ahmad Abdul Hamid, *The Implementation of Islamic Law in Contemporary Malaysia : Prospects and Problems* (2009).
[202] Riaz Hassan, "Power and Piety: Religion, State and Society in Muslim Countries" (the 15th Annual International Conference on Islamic Studies on 'Harmony in Diversity: Promoting Moderation and Preventing Conflicts in Socio-Religious Life,' Manado, Indonesia, 2015), https://www.unisa.edu.au/Documents/EASS/MnM/working-papers/Riaz%20Hassan%20Power%20and%20Piety%20Religion,%20State%20and%20Society%20in%20Muslim%20Countries%202015%20paper.pdf.

There has been a constant federal-state tension over religious authority in Malaysia.[203] However, the role of state-level religious agencies has diminished since the Islamization project of the 1980s. The federal government, under the leadership of JAKIM (Jabatan Kemajuan Islam, or Islamic Development Department), the central religious authority, managed to minimize a 'separatist' tendency apparent in individual state level religious authorities. According to Hamayotsu, this has prevented them from building an entirely separate religious-legal regime based on their own localized interpretation in each State.[204] This strategy proved to be an essential part of the success in Islamic finance project discussed in this dissertation.

Malaysia is neither an Islamic state where the law is ultimately derived from Islam nor a secular state. It is the Federal Constitution and not Islamic Law that becomes the ultimate source of legal and constitutional authority. The relationship between the Federal Constitution and Islamic law is entirely different from the Pakistan-type model of Islamic State. Nonetheless, Islam does have constitutional status in Malaysia. The Constitution (specifically, Article 3) establishes Islam at the state religion of Malaysia.[205] Therefore, Tom Pepinsky defines Malaysia as an Islamist state rather than an Islamic state.[206]

The place of Islam within the state system differentiates Malaysia with another country, for instance, Indonesia, which rejects the supremacy of Islam over other religions. Under Indonesian law, the state through the Ministry of Religion is responsible for all manner of norms, standards, and procedures for the organization and functioning of other officially recognized faiths. In Malaysia, Islam and Islamic organization receive preferential treatment from the government.

Sharia courts exist for Muslims in parallel operation of civil courts. However, Islamic law is enacted only for Muslims and has no relevance for non-Muslims whatsoever. The institutionalization of Sharia court, interestingly, has come with 'modernization' of the Sharia

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[203] Kikue Hamayotsu, "Politcs of Syariah Reform: The Making of the State Religio-Legal Apparatus," in *Malaysia: Islam, Society and Politics: Essay in Honour of Clive S. Kessler/ Edited by Virginia Hooker and Norani Othman*, ISEAS Series on Islam (Singapore: Institute of Southeast Asian Studies, 2003), 55–79.

[204] Kikue Hamayotsu, "Once a Muslim, Always a Muslim: The Politics of State Enforcement of Syariah in Contemporary Malaysia," *South East Asia Research* 20, no. 3 (2012).

[205] "Constitution of Malaysia," n.d., http://confinder.richmond.edu/admin/docs/malaysia.pdf.

[206] Tom Pepinksy, "Is Malaysia an Islamic State," accessed April 25, 2018, https://tompepinsky.com/2012/10/26/is-malaysia-an-islamic-state/.

mechanism. This modernization process is not a novel thing. It is a continuation of the modernization process previously conducted under the British colonial regime. This type of modernization resulted in a selective approach of Islamic law where the 'draconian' elements of the Sharia, such as traditional capital punishment, were removed and rejected.[207]

The role of Islam in the nation and state building has always become contestation among Malaysian Muslims. The expansion of modern state institutions is highly political. On the one hand, there is no evidence to suggest that an Islamic vision of state motivated the founding fathers of independent Malaysia. The Muslim politicians -Tunku Abdul Rahman, Tun Abdul Razak, and Tun Dr. Ismail- who played a significant role at that time approached the complexity of multi-ethnic Malaya as liberal and English-educated Malays. On the other hand, a small segment of the Malay community represented by the Islamic Party of Malaysia (PAS) who consistently argue for an Islamic state. Their argument is the political power in Malaysia must be in the hands of the Muslims. According to their understanding of Sharia, non-Muslims can perform various administrative and bureaucratic roles, but under the direction of Muslim power holders. Contrary to the liberal-minded of Malaysia's founding fathers, PAS leaders readily use the idiom of religion to engage with the process of state building. [208]

Malaysian capitalism

The British Colonialism introduced capitalism to Malaya through the establishment of plantation and mining economy. Initially, the British maintained the 'non-intervention' trade relations with Malay states. However, as Britain's need for raw materials supply, particularly tin, had increased the British went for further incursion in Malay states' domestic affairs in order to safeguard trade monopoly. Furthermore, there was an opportunity presented by invitation from Raja (Prince) Abdullah of Perak to aid him in his conflict against another prince for the throne in 1873. In his book, Azlan Tajuddin explains the transformation of Malaysian economy in detail. [209]

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[207] Hamayotsu, "Politcs of Syariah Reform: The Making of the State Religio-Legal Apparatus."
[208] Muzaffar, "Power Sharing: The Significance of the Malaysian Experience for Muslims in Multi-Religious Society."
[209] Azlan Tajuddin, *Malaysia in the World Economy (1824-2011) : Capitalism, Ethnic Divisions, and "Managed" Democracy* (Lanham: Lexington Books, 2012).

Based on this invitation, the British made some treaties with the ruler of the Malayan state in the form of residential system. The residential system gave Malaya prince assistance and support in their conflict with other states (protectorate), and at the same time gave the British monopoly in the tin trade. The residential system was vital in the transformation of Malay political economy structure. It strengthened the prestige and position of the Sultan, and effectively marginalized the powers of the various local or village leaders.[210] The residential system also created salaried positions for the multiple members of the aristocrats, thereby effectively taking away their traditional prerogatives in controlling local trade.[211] The old Malay government machinery soon gave way to modem western style bureaucratic administration with a centralized structure under the Resident. These transformations, along with the enforcement of standardized British-type laws, helped shield the processes of tin extraction and transportation in the Malay States from any civil disruptions.[212]

Furthermore, the residential system created a supportive land lease and labor tax laws in response to the demands for agriculture and mining. The British declared that all lands were vested in the ruler. According to Tajuddin:

> In the decade between 1879 and 1889, General Land Regulations based on standardized leaseholds were introduced in Perak, Selangor, and Negri Sembilan. Malays in rural areas were now required to register the lease of their lands from the new government for 999 years in return for quit rent. Lands not actually cultivated or occupied were to become 'state land'. In effect, the land was transformed into private property with prescribed rights and obligations, which greatly enhanced production processes and the management of revenues in British hands. It facilitated the growth of the tin trade as well as provided the impetus for greater agricultural mass production, particularly pepper, gambier, tobacco, sugar, tea, coffee, and later, rubber and palm oil. For the Malays, the new land laws enabled the precipitation of sale and losses of their lands to Chinese and Indian moneylenders, since many had placed their lands as collateral for loans, as well as to plantations and land agents, who regarded lands as a commodity. [213]

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[210] J. M Gullick, *Malay Society in the Late Nineteenth Century the Beginnings of Change* (Singapore: Singapore, 1987).
[211] N. J Ryan, *The Making of Modern Malaysia and Singapore : A History from Earliest Times to 1966*, 4th ed., rev.. (Kuala Lumpur: Kuala Lumpur, 1969).,162).
[212] Ryan.
[213] Tajuddin, *Malaysia in the World Economy (1824-2011) : Capitalism, Ethnic Divisions, and "Managed" Democracy*.

Furthermore, various types of labor legislation were introduced organizing wage labor and revenue collection for the state. This legislation had profound impact in establishing the dominant role of the Chinese Malaysian in the economy. Under this system, Chinese towkays (headmen or 'advancers') were responsible for the recruitment and maintenance of their workers into the Malay states. They were also the ones who provided these workers with expensive supplies, in which loans were usually made at double the market rates as 'payments' for their boarding and transport. Although the British controlled the overall tin production process, such a profitable enterprise allowed Chinese firms to dominate the tin industry in the early years of British colonial administration.[214]

Since tin provided the mainstay of the new capitalist economy, lands in which potential tin deposits could be found were strictly dealt with in terms of clear and uniformed laws. The commodification of land and labor in the Malay States was a process that was highly integrated with the use of monetary funds to inject mercantile investments in trade and production. Large-scale tin mining also fueled other activities of the modem capitalist economy into the Malay States such as retail, consumer durables, and supplies. It became largely responsible for the urbanization process in this region, which contributed to the growth of Singapore and the cities on the western coast of the Malay Peninsula.[215]

Tin production serviced the needs of a growing industrial manufacturing base in the west, in which case, capital-friendly land and labor laws became important antecedents to the consolidation of British economic interests in the Malay states. This system also consolidated the labor structure of the colony. Drabble noted that the trading system in the Malay States, Singapore, and northern Borneo throughout the nineteenth century was characterized by a three-tier participatory structure. At the top is a group of largescale entrepreneurs dealing in imports and exports, consisting mainly of Europeans and later in the case of Singapore, some Chinese. This group, backed by huge capital, dealt mainly in the vast bulk of wholesale items. The second group is made up of medium scale bazaar-type traders, situated usually in the ports in the form of small import-export firms. Chinese merchant houses, and to some extent limited

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[214] Tajuddin.
[215] Azlan Tajuddin, *Malaysia in the World Economy (1824-2011) : Capitalism, Ethnic Divisions, and "Managed" Democracy* (Lanham: Lexington Books, 2012).

Indian companies, performed many of these groups' activities goods collection and distribution and retailing. The third group consists mainly of on-the-ground, small peddlers and market traders. This group, which comprises mostly of Malay and other indigenous peoples, operated throughout the Malay world in the ports as well as in the hinterlands of deep forests and jungles. Goods are usually primary products to be exchanged for small quantities of imports. Interdependence of the system is reflected in the finance and credit networks that filtered down from the top through banks and manufacturers.[216] This structure also explains the persistence of ethnic tension in the post-colonial era.

Capitalist incorporation of the Malay States and the northern Borneo regions was a result of two kinds of social process under the residential system. One was the redefinition of land in terms of capital in order to generate revenues for both individual entrepreneurs and the state and the other one was the establishment of a wage system. Under Residential system, laws were formulated to enable the efficient transfer of landed property into the hands of individual capitalists. Not only was land now legally owned as individual property, the state also managed its transactions through laws that secured its expropriation of minerals and resources. A wage system organized labor forces for purposes of extracting surplus value to facilitate the newly emerging capitalist production in the Malay states. The shortage of labor compelled the British to recruit labor from overseas, which later on influence the ethnic relations in Malaysia. The relation between ethnics in Malaysia is dominated by the socio-economic structure of Malaysian capitalism.

Both processes were significant landmarks in Malay political economic history since they became the crucial transitory factors that ushered the feudal Malay world into the world capitalist economy. They also became the turning points of active Malay involvement in the regional economy.[217] Moreover, the social transformation of Malay society was a result of colonial encroachments. The transformation was not a process resulting from internal dynamic forces but rather from coercively external, top-down factors. In the late nineteenth century,

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[216] John H. Drabble, *An Economic History of Malaysia, c.1800-1990: The Transition to Modern Economic Growth*. London: Macmillan Press and New York: St. Martin's Press, 2000. xxiii + 320 pp. $75 (cloth), ISBN: 0-312-23077-X. as quoted in Tajuddin.

[217] Tajuddin.

further consolidation of British capitalist interests was realized through the unification of some of the more affluent Malay states into a formal and autocratic colonial state.[218]

The introduction of a capitalist economy led to profound social change. Malay states had become an important source of agricultural and forest commodities for export, and a market for textiles, hardware, and other foreign goods. These developments led to extensive commercialization of the economy, which continued after the formation of independent Malaysia. The first decade of Malaysian independence was a period in which the elite classes solidified their positions and utilized the state apparatus to advance their political economic interests with the support from Chinese entrepreneurs and foreign investment.[219]

In the 1970s, Malaysia replicated the developmental state of Japan and South Korea in which the government heavily involved in trade and industrial policies. In this 'Look East' policy, the government of Malaysia chose strategic industries to be supported through generous allocated credit. State-owned enterprises and government-linked companies mostly ran these industries. However, Malaysia's version of the developmental state was more open to foreign investment by multinational enterprises. Moreover, the state also encouraged the development of public equity markets, which provided domestic firms with and alternative source of capital.[220]

Starting 1980s, Malaysia's Barisan Nasional coalition under Mahathir Mohamad had relied more on an alliance between the Malay masses and a class of the new Malay entrepreneurs. Chinese entrepreneurs were still important, but the government had continuously tried to limit their political role. The ruling Malay government understood that the creation of an indigenous Malay entrepreneur class was essential to sustain its regime. However, the government preferred to take an instant method rather than nurtured genuine entrepreneurs. Many of these Malay entrepreneurs were not professional managers. They were senior civil servants who were appointed to senior positions in the Malaysian business group. This strategy gave enormous benefit to Mahathir. Besides fulfilling the shortage of qualified

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[218] Ibid.
[219] Ibid.
[220] Michael Carney and Edo Andriesse, "Malaysia: Personal Capitalism," in *The Oxford Handbook of Asian Business System*, ed. Michael A. Witt and Gordon Redding (Oxford University Press, 2014).

manager, the usage of bureaucrats enabled the Prime Minister to have personal control over the businesses. [221]

Favoritism in economic and social policy ensures support from ordinary Malays; favoritism in corporate and financial policy ties the new wealthy Malays to the regime.[222] At the same time, Mahathir had started the privatization process of Malaysia's economy. In overall, the capitalist system of modern Malaysia can be described as a combination of developmental state and liberal market economies infused with personalized patron-client relationships. This patron-client relationship, particularly during the Mahathir regime, was very significant for the development of Islamic insurance in Malaysia. The following sections discuss this correlation in further details.

Political actors in Islamic politics

The following paragraphs provide a brief map of the actors of Islamic politics in Malaysia particularly on their position on to the institutionalization of Islamic insurance. According to Meredith Weiss, Islamization in Malaysia, in general, created a fragmentation of political society into three blocks, 'as the debate over the role of religion inevitably had an impact upon the possibilities for democratization and market-led modernization.'[223] Weiss mentions the three block consists of those who desired Malaysia to become a secular state represented by the Chinese-dominated Democratic Action Party (DAP), those who imagine Malaysia as a democratic state imbued with Islamic values, but retaining secular laws and institutions, coalesced around the communally organized UMNO and its partners in the ruling BN coalition, and those who called for establishing an Islamic state with full implementation of Sharia of the Parti Islam SeMalaysia (PAS, Pan-Malaysian Islamic Party). Regarding Islamic insurance, three important actors need to be added beside these three political groups; the civil society groups (ABIM and Islamic NGOs), epistemic community and the insurance industry.

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[221] Ibid., page 162-163.
[222] Pepinsky.
[223] Weiss.

The governing *Barisan Nasional* coalition (BN, National Front) comprises about a dozen parties. Incorporated in 1974, this coalition is an expansion of a tripartite union called the Alliance that contained three race-based parties, UMNO, the Malaysian Chinese Association (MCA) and the Malaysian Indian Association (MIC). The Alliance was handed power by the British colonial government when Independence was declared in 1957. The BN is headed by the United Malays National Organization (UMNO), with Mahathir Mohamad (1981-October 2003) and then Abdullah Ahmad Badawi (November 2003) as prime minister. UMNO is secular nationalist, though with increasing attention to Islamization since the 1970s; it is the linchpin of BN, and the head of UMNO has always been head of government. UMNO had historically catered to Malaysian Chinese, Malaysian-Indian, and foreign business interests.[224]

Bridging the gap between the heightened religiosity of the society and electoral politics have been Islamic NGOs. Most prominent among these in terms of both size and political impact has been *Angkatan Belia Islam Malaysia* (ABIM, Malaysian Islamic Youth Movement). The Islam Malaysia (ABIM, Malaysian Islamic Youth Movement). The organization's ventures include a network of Islamic schools that annually educate 20,000 students, a corporate arm (*Koperasi Belia Islam*), and substantial property holdings. ABIM's nationwide complex of state and district branches stretches down to the grassroots, with a 1,000 strong staff and around 60,000 members.

Most members are university graduates, often brought into the dakwah (Islamic proselytization) movement. Most have been beneficiaries of federal affirmative-action policies that benefit Bumiputera, or Malays and other indigenous peoples, in university admissions, career advancement, and other areas. ABIM has produced leaders of PAS, UMNO, and the more recently formed *Parti Keadilan Nasional* (Keadilan, or National Justice Party; multiracial but Malay-dominated; centered around former deputy prime minister Anwar Ibrahim and headed by his wife, Wan Azizah Wan Ismail). Among them is Anwar Ibrahim helped found ABIM in 1971, then led the organization from 1972 until he resigned to join UMNO; past PAS president (until his

[224] Ibid.

death in 2002) Fadzil Noor; his deputy and successor Abdul Hadi Awang; and Keadilan supreme council member Ghazali Basri.[225]

The Malay opposition parties (DAP & PAS*),* by contrast, has evolved toward two divergent positions on the issue of Islamic statehood and democracy. While the PAS has only about 15% electoral support, it has managed to push the UMNO to implement elements of its nationalist-religious agenda. Islamic revivalism has brought heightened emphasis on Islamic rituals, implementation of Islamic legal codes, and strengthening of Islamic praxis in all areas of social, political, and economic life. For example, in the two states PAS governs, the party has required that Muslim women cover their heads, restricted gambling and the sale of alcohol, and tried to implement *hudud/*criminal law (though barred from doing so by the Malaysian constitution).

Meanwhile, the DAP is claimed to be multi-racial and center-left Malaysian political party advocating for social democracy and secularism. The DAP usually draws much of their support from secular and liberal voters with a stable electorate from voters of big cities, coastal regions, professional middle-class, and working class. The party's strongholds are primarily in the urban and semi-urban areas of Penang, Perak, Selangor, Negeri Sembilan, Johor and the Federal Territory of Kuala Lumpur. In the 2018 Malaysian general election, DAP contested in 47 federal constituencies and won 42 seats and 101 out of 104 state seats contested, most under the ticket of its ally People's Justice Party (PKR), representing a win rate of 95%, the highest among the major political parties contesting.[226]

Foreign players dominate Malaysia insurance industry. Although they are economically dominant, they do not have direct political influence on the development of Malaysia insurance structure. On the contrary, the government through its central bank, Bank Negara Malaysia (BNM) has strictly regulated this sector. Access to the Malaysian insurance market is very restricted, BNM issues a limited number of insurer licenses. No direct conventional insurance license has been issued since the 1970s. New reinsurance, Islamic insurance and Islamic re-insurance licenses have been issued from time to time since 1995 to meet specific objectives to enhance domestic reinsurance capacity and further develop the Islamic insurance industry. Seven

[225] Ibid.
[226] Ibid.

reinsurance licenses (one life reinsurance license and six general reinsurance licenses) were issued between 1995 and 2007 and twelve Islamic insurance and Islamic insurance licenses were issued between 2005 and 2010. Not included is the special license for the government backed financial guarantee insurer established in 2009.

Foreign ownership of Malaysian insurers is restricted. The foreign equity limit for insurers is 70 percent. A foreign equity limit above 70 percent will be considered on a case-by-case basis, particularly for players that can facilitate consolidation and rationalization of the general insurance industry. The foreign equity limit for reinsurers is 70 percent. Reinsurers are also allowed to be established as branches. The foreign equity limit for Takaful operators is 70 percent. There is no foreign equity limit for Islamic re-insurance operators. There is a clear trend towards consolidation of insurance industry players in the Malaysian market, led by the general insurance sector.[227]

In Malaysia, the insurance industry has been regulated by Bank Negara Malaysia since 1 May 1988. Prior to that, the Ministry of Finance regulated the industry as per the Insurance Act 196343, which outlines the main set of rules and regulations governing operations of insurance business in the country. The Insurance Act 1996 subsequently replaced this Act. The regulation of the insurance industry by the Central Bank also involves policy development, administration and enforcement of the Insurance Act 1996 governing the insurance industry, carrying out the actuarial function, supervision of insurance licensees, consumer education and complaints handling. The close supervision of solvency and market conduct along with a strengthened regulatory framework enforced in the 1990s helped to enhance the professional standards in the insurance industry and consumer confidence.[228]

There are currently 47 licensed insurance companies operating in Malaysia – general, life, composite and Takaful license holders, out of which close to 70% of the units contain stakes held by foreign shareholdings. Domestic banks either have their own insurance operators, JV with a foreign partner or banc-assurance agreement to offer complete range of general and life

[227]International Monetary Fund, *Malaysia: Publication of Financial Sector Assessment Program Documentation-Detailed Assessment of Observance of Insurance Core Principles* (Washington, D. C.: 2013), https://www.imf.org/external/pubs/ft/scr/2013/cr1357.pdf.
[228] Thanasegaran and Shaiban.

products. 15 Takaful companies set up Malaysia Takaful Association (MTA) in 2008. This organization is dedicated in promoting the interest of its members and to supervise the exercise of self-regulation within the Takaful industry. Moreover, they signed inter-Takaful operator agreement to set a common standard among all operators to regulate on and control matters related to pre-contract examination for agents, agency registration system and code of ethics, and compliance of the general Takaful tariff for motor and fire businesses.[229]

Most of the study on finance focus the roles of investors, lenders, analysts, advisors, actuaries, and other skilled financial professionals informing and reproducing financial and other markets. The unique aspect of Islamic finance is in the prominent role of epistemic community, which consist of Sharia professionals, jurists, and adviser in the law-making process. Together with practitioners, they formulate rules and regulation on Islamic finance. They are not the traditional village religious authority, but they are an urban class of Sharia professional and government bureaucrat who are increasingly armed with educational credentials from local and foreign universities, they are promoting a more rational scientific approach to Islam and treating rural Islam as mystical and ritualistic. The establishment of International Islamic University of Malaysia (IIUM) has been very central in this process. IIUM and the International Center for Education in Islamic Finance (INCEIF) has produced a skilled pool of graduates available for expanding the Sharia bureaucracy particularly at the federal level.[230]

Being amongst the Islamic insurance elites

The development of the Islamic insurance industry in Malaysia in the early 1980s was inspired by the prevailing needs of the Muslim public for a Sharia-compliant alternative to conventional insurance, as well as to complement the operation of the Islamic bank that was established in 1983.[231] Islamic insurance becomes a new venue for both individual and company

[229] Milliman, *Global Takaful Report 2017: Market Trends in Family and General Takaful*.
[230] Daromir Rudnyckyj, "Islamic Finance and the Afterlives of Development in Malaysia," *PoLAR: Political and Legal Anthropology Review* 37, no. 1 (2014 2014).
[231] Bank Negara Malaysia, “Malaysian Takaful Industry 1984-2004” (Kuala Lumpur, 2004), https://www.bnm.gov.my/files/publication/tkf/en/2004/booklet.en.pdf.

for investment, joint ventures, and alternative insurance sector with Islamic characteristics.[232] As an individual, a Muslim has the opportunity to invest in their family's future and at the same time, he or she receives financial protection. Meanwhile, an experienced international insurance company can access insurance market in Malaysia by joining with the domestic Islamic insurance company to provide Islamic insurance services. All processes have been carefully planned and directed by the state.

History and development

In June 1972, the National Fatwa Committee declared that the concept of conventional insurance contravened the rules of Sharia.[233] Insurance transaction contains elements of interest, gambling, and speculation, which are prohibited in Islam. In 1982, the Task Force to Study the Establishment of an Islamic Insurance Company in Malaysia was formed by the order from Prime Minister Mahathir Mohamad. This Task Force has a task to investigate the possibility of launching Islamic insurance as a complement to Islamic banking. Datuk Mohd Fadzli Yusof, the current chief executive officer of Syarikat Takaful Malaysia Sdn. Bhd. was one of the members of this task force. Later, when Takaful Malaysia first started operation in 1984, Fadzli was made the chief executive officer, a position he has held until today. He is known as the first Takaful man in Malaysia due to his prominent role in initiating Islamic insurance.[234] Following the recommendations of the Task Force, the Malaysian Parliament enacted the Takaful Act 1984, thus giving birth to the Takaful Scheme in Malaysia.[235]

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[232] DBS Group Research, *Malaysian Insurance Sector* (DBS, 2017), https://www.dbs.com.sg/treasures/aics/pdfController.page?pdfpath=/content/article/pdf/AIO/092017/170907_insights_changes_in_ownership_of_insurance_firms.pdf

[233] National Fatwa committee in June 15, 1972 declared,"..Life Insurance operated by the present-day life insurance companies is transaction containing the elements of al-Gharar, al-Maisir, and al-Riba and as a consequence its contract is void; therefore HARAM.. Dato' Mohd Fadzli Yusof, "Shariah Overview of Takaful" (paper presented at the The International Takaful Summit, London, 30 June, 2009), https://issuu.com/takafulprimer/docs/1015-fadzli."

[234] Hasni Mohd Nasir, "Fadzli - the First Takaful Man," *the Star Online* (15 September 2003), accessed 15 January 2017, https://www.thestar.com.my/business/business-news/2003/09/15/fadzli-150-the-first-takaful-man/#4EvG3rvZqozViWtm.99.

[235] The report dated 11th May 1984 accepted by the Malaysian Government inter-alia concludes that ,"..6.1.1 From detailed description outlined in the various chapters, a number of conclusion can be considered as follows: a) The Task Force is confident that a company whose operation shall be based on the concept of Takaful and *Mudharabah* is viable to be established in Malaysia… besides its participant will have opportunity to save, invest, and earn profit

Malaysia has developed Islamic insurance gradually within three phases since that moment. The first phase (1984-1992) started by the enactment of the Takaful Act 1984, the establishment of Syarikat Takaful Malaysia Sdn. Bhd. (the first and the sole Islamic insurance operator in the country) and placement of the basic infrastructure for the industry. In this phase, the government focused its effort on setting the foundation for Islamic insurance by providing basic regulation. The main investors/shareholders of Syarikat Takaful Malaysia Sdn. Bhd. during this phase were an Islamic bank and state religious councils and foundations, and the customers were mainly Muslims. The products offered were quite limited consisted of motor, fire and mortgage Islamic insurance. Similarly, the investment avenues were confined to Islamic deposits and government Islamic securities.[236]

The second phase (1993-2000) marked the introduction of competition, with MNI-Takaful Sdn. Bhd. (now known as Takaful National Sdn. Bhd.) entering the scene as Islamic insurance operators. In 1993, MNI Takaful was licensed and has since been operating in Malaysia. This latter insurer currently focuses on enhancing customer services technology and developing new marketing channels, e.g., policyholders' services through post offices. Malaysia National Insurance Company, the largest local insurance company, currently owns about 80 percent of the shares of MNI Takaful. This phase also witnessed greater regional cooperation amongst Islamic insurance operators, with the establishment of the ASEAN Takaful Group in 1995 and ASEAN Retakaful International (L) Ltd. in 1997 to facilitate Islamic re-insurance arrangements in the region.[237] They have a wider range of investment instruments issued by the Government and the private sectors. There was a broad range of products features with more than 71% share of Family Takaful products of the dominated market.

Next, the third phase (2001-2010) then began in tandem with the introduction of the Financial Sector Master Plan (FSMP) by the Central Bank, which has as its objectives the enhancement of the capacity of Islamic insurance operators and the strengthening of the legal,

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based on Mudharabah principle, b)..Under the system of Islamic insurance, installments/contributions paid by participants shall be made as tabarru'-not on the basis of buy-and-sell in view that Islamic law accept tabarru and hence the transaction is permissible." As mentioned in Yusof.

236 Bank Negara Malaysia, "Malaysian Takaful Industry 1984-2004."

237 Haemala Thanasegaran, "GROWTH OF ISLAMIC INSURANCE (TAKAFUL) IN MALAYSIA: A MODEL FOR THE REGION?," *Singapore Journal of Legal Studies*, July 2008, 143–164.

Sharia and regulatory frameworks. The Malaysian Takaful Association (MTA) in 2002 was established during this phase. The association was formed as an association for Islamic insurance operators to improve industry self-regulation through uniformity in market practice and to promote a higher level of cooperation amongst the operators in developing the industry. As at February 2008, there were eight registered Islamic insurance operators in the country, namely Syarikat Takaful Malaysia Berhad, CIMB Aviva Takaful Bhd., Hong Leong Tokio Marine Takaful Bhd., MAA Takaful Berhad, Takaful Ikhlas Sdn. Bhd., Prudential BSN Takaful Bhd., HSBC Amanah Takaful (Malaysia) Sdn. Bhd., and Etiqa Takaful Bhd. In addition to this, the Central Bank in September 2006 approved the licenses of 2 additional Islamic re-insurance companies, namely Munich Re and MNRB Holding Bhd. The policy was intended to strengthen the institutional infrastructure of the Malaysian Islamic insurance industry as well as synergize the overall financial sector. Also, particularly since 2004, this phase witnessed the increasing interest from the non-Muslim costumers with different expectations, experiences, and demands toward Islamic insurance.[238]

Furthermore, the Financial Sector Master Plan (a 10-year plan to be implemented in 3 phases) was launched by the Central Bank on 1 March 2001 and provided the blueprint for the development of the financial sector (of which Islamic insurance is a part). At its core are recommendations aimed at developing a competitive and dynamic financial system resilient to a more challenging and globalized environment ahead.[239]

Malaysia has been developing Islamic Insurance of Takaful since 1984 with high government commitment and top-down approach comprehensively and pragmatically. With support from the business sector and universities particularly IIUM (International Islamic University of Malaysia), the Central Bank has managed to gradually develop Islamic insurance industry in Malaysia. In 2016, total premiums and contributions of Takaful sector increased of Takaful by 4.4% to RM 61.3 billion or USD 14 billion (2015: +4% to RM 58.7 billion), while combined insurance and Takaful assets expanded by 5% to RM 277 billion or USD 64 billion (2015: +5.7% to RM 263.8 billion). There were also 55 insurers and Islamic insurance operators, including

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[238] Bank Negara Malaysia, “Malaysian Takaful Industry 1984-2004.”
[239] Thanasegaran, “GROWTH OF ISLAMIC INSURANCE (TAKAFUL) IN MALAYSIA: A MODEL FOR THE REGION?”

reinsurers and Islamic re-insurance operators, in the industry as at end-2016.[240] Altogether, Malaysia has been contributing by 70% of the total regional market of Southeast Asia and 13% of the global market of Takaful respectively.

Figure 3-1: List of Islamic Insurance Operator in Malaysia

	Name of company	**Year**	**Ownership**
1	Syarikat Takaful Malaysia Berhad	1984	Foreign (F)
2	Takaful Ikhlas Sdn. Bhd	2003	Local (L)
3	CIMB Aviva Takaful Berhad	2005	L
4	Prudential BSN Takaful Berhad	2006	L
5	HSBC Amanah Takaful (Malaysia) Sdn.Bhd	2006	L
6	Hong Leong MSIG Takaful Berhad	2006	L
7	MAA Takaful Berhad	2006	L
8	Etiqa Takaful Berhad	2007	L
9	AmFamily Takaful Berhad	2010	L
10	Great Eastern Takaful Berhad	2010	F
11	AIA AFG Takaful Bhd.	2010	L
12	AIA Public Takaful Bhd	2010	L

Source: Bank Negara Malaysia, October 2018

Figure 3-2: List of Islamic Re-Insurance Operator in Malaysia

	Name of company	**Ownership**
1	ACR Retakaful Berhad	Foreign
2	MNRB Retakaful Berhad	Local
3	Munchener Ruckversicherungs-Gesellschaft (Munich Re Retakaful)	Foreign
4	Swiss Reinsurance Company Ltd. (Swiss Re Retakaful)	Foreign

Source: Bank Negara Malaysia, October 2018

240 Malaysia. Accessed date: August 7, 2017.

Regulatory framework

Those successes cannot be separated from the constant effort by the Malaysia government to institutionalize its Islamic insurance industry through Public-Private Partnership scheme. Mark Smith who assessed the contemporary state of Islamic finance in Malaysia said, "Malaysians have seen consistent high-level government support of the industry within the country and internationally, are exposed to large marketing campaigns, and have seen Islamic banks on the main street for a generation. In such an environment the level of wholesale suspicion of something new has largely been erased, though increased customer education about the products remains a challenge."[241]

Malaysia is the first country who created specific and separate Islamic insurance regulation from conventional insurance, the Takaful Act 1984. The role of Islamic insurance within the Malaysian secular common law system is clearly delineated by the Malaysian Federal Constitution.[242] In Malaysia, Islamic insurance is considered to be a part of mainstream mercantile law, and hence a part of civil law and subject to the civil court structure of the country. Therefore, the Federal Parliament has jurisdiction to legislate over it (as it has done via the Takaful Act 1984), as opposed to being regulated by Sharia law and the Sharia courts. At this moment, only Saudi Arabia and Sudan (and Iran) take the conservative approach of treating Takaful as being a part of Sharia.[243]

The Takaful Act 1984 states that *Bank Negara* (the central bank of Malaysia) was appointed to regulate Takaful insurance operations and to monitor the compliance of Takaful insurers with the Sharia. Section 54 of the act entrusts the Central Bank with the responsibility of administering the Act, whereby the Governor of the Bank is also the Director General of Takaful.[244] Moreover, this is apparent from the combined effect of Articles 73, 74, 75, 121(1), 121(1A), and the 9th Schedule of the Federal Constitution of Malaysia and is in line with Malaysia

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[241] Smyth, in *Contemporary Islamic Finance: Innovations, Applications, and Best Practices*.
[242] Haemala Thanasegaran, "Growth of Islamic Insurance (Takaful) in Malaysia: A Model for the Region?," *Singapore Journal of Legal Studies* (2008).
[243] Ibid.
[244] BNM, *Structure of Malaysia Takaful-Takaful Act 1984* (Kuala Lumpur: BNM, 1984), http://www.bnm.gov.my/documents/act/en_takaful_act.pdf.

being a moderate Islamic country, with Sharia being confined to personal and inheritance matters.[245]

However, Sharia still plays important part of Islamic insurance in Malaysia. The operation of Islamic insurance in Malaysia must conform to Sharia or Islamic rulings on the commercial transaction. Unlike health care sharing ministries or other non-profit schemes, Islamic insurance is confined in the commercial or private sector. As a result, its operation is regulated based on the Islamic commercial profit-sharing principle of *Al-mudharabah*. Al-mudharabah is recognized as the commercial profit-sharing contract between the providers of funds for a business venture (participants) and the entrepreneur who actually conducts the business. The principle of the Al-mudharabah contract has been successfully modified and developed into the Malaysian model, where the participant of an Islamic insurance product is entitled under the contract to enjoy a return on the contribution or premium paid in consideration for participating in the product. This contrasts with the *Al-wakalah* principle, which is based on the idea that the operator, acting as an agent of the participants, can charge its management expenses on the Islamic insurance contributions or premium paid. [246]

Islamic insurance is defined in section 2 of the Act as a scheme based on brotherhood, solidarity and mutual assistance whereby the participants mutually agree to contribute to providing for mutual financial aid and assistance in case of need. The Act also classifies Islamic insurance business into the family solidarity business, which is defined as Islamic insurance for the benefit of the individual and his family, and general business, which is defined as all Islamic insurance business that is not family solidarity business. In the terminology of conventional insurance, family solidarity business refers to life insurance while general business is equivalent to general insurance.[247]

Family Takaful is like an endowment policy. A participant decides on the maturity period, the amount of annual contribution (provided it is above the minimum amount set by the company), and the frequency of contributions. The money goes into two different accounts,

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[245]Ramin Cooper Maysami and W Jean Kwon, "An Analysis of Islamic Takaful Insurance: A Cooperative Insurance Mechanism," *Journal of Insurance Regulations* 18, no. 1 (Fall) (1999).
[246] Mohit Anand, "Islamic Insurance in Malaysia: Insights for the Indian Insurance Industry," *Singapore Journal of Legal Studies* (2014).
[247]BNM.

namely the Participants' Account (PA) (a savings and investment account) and the Participants' Special Account (PSA) (which is for contributions made for the purpose of *Tabarru* or donation), whereby the participants agree upon to relinquish as donation a certain portion of their Islamic insurance installments as contribution to a common pool out of which is paid the compensation as agreed upon in the contract of Islamic insurance. In this way is realized the goal of assisting and helping the participant who may suffer some loss. Money from both accounts is invested in accordance with Islamic principles. The General Takaful protects participants against losses from personal accidents and loss or destruction of property. The contract specifies the amount of contribution that the participant must make. All contributions are paid into the General Takaful fund.

Part of the fund is used to cover the expenses while the rest of the fund is invested like in family Takaful. Profits in the fund are then shared between the company and the participants. The registration of Islamic insurance operators is covered in section 8 of the Takaful Act 1984. Section 8(5) states that the applicant must satisfy the Director General of Takaful that the aims and operations of the Islamic insurance business will be in accordance with Sharia, and that the Articles of Association provides for the setting up of a Sharia Supervisory Council.

According to Thanasegaran, the concern shown in the Islamic insurance contract to specify every detail is not only Islamic but also a definite improvement on the existing nature of conventional insurance contract. However, despite every effort to spell out details of the Islamic insurance contract, there may still be some uncertainties. For example, how much the Islamic insurance company must pay to settle a claim under a third-party motor policy *may* only be known after actual happening. Such uncertainties are inherent in the contract of insurance and are condoned under the doctrines of necessity and public interest.[248]

Like conventional insurance, the issues of "insurable interest" and *uberrimae fidei* (of the fullest confidence) are essential in the Islamic insurance. Thanasegaran further explain, "The nature of family Takaful is such that the issue of insurable interest is automatically taken care of; the participant himself is both the insured and the policy-holder. In case of the General Takaful (fire, accident, motor, etc.), although the Takaful Act 1984 is silent on insurable interest, yet the

[248] Thanasegaran.

general provisions of the Contract Act 1950 against wagering contracts may be applied to these contracts requiring the participant to show enough interest in the subject-matter, both at the inception and the time of loss."[249]

The principle of *uberrimae fidei* is emphasized equally under the Islamic law of contract and its rules regarding honesty, full disclosure, truthfulness and utmost good faith. Non-compliance of these makes the contract un-enforceable and it applies fully to any Islamic insurance contract. As the Takaful Act 1984 does not state the whole of the law governing an Islamic insurance contract, it is presumed that section *5* of the Civil LAW Act 1956 applies. This section says *inter alia* that "in all questions or issues with respect to life, and fire insurance, and with respect to mercantile law generally, the law to be administered shall be the same as in England."[250]

The Malaysian government has however taken steps over the years to enhance the industry in terms of its infrastructure and education. In 2003, it launched a 10-year Consumer Education Program to educate consumers of their rights and responsibilities arising under insurance and Islamic insurance contracts. This policy was followed by the amalgamation of the Insurance and Banking Mediation Bureaus into the highly effective Financial Mediation Bureau in 2005 which handles most of the insurance and Takaful complaints to date. The Law Harmonization Committee was in turn established in 2010 to facilitate a more conducive legal system to achieve certainty and enforceability of Malaysian Islamic finance laws. This law was followed in 2011 by the Central Bank's Sharia Governance Framework for Islamic Financial.[251]

The Malaysia government undertook several regulatory reforms to enhance the role of the critical organs responsible for executing Sharia compliance. In 2013, the government issued the Financial Services Act 2013 (Malaysia) and the Islamic Financial Services Act 2013. Both these statutes came into effect on 30 June 2013 following a much-awaited repeal of their predecessors, the Insurance Act 1996 (Malaysia) and the Takaful Act 1984 (Malaysia).

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[249] Ibid.

[250] Syed Khalid Rashid, "Islamization of Insurance-a Religio-Legal Experiment in Malaysia," *Religion and Law Review* 2, no. 1 (1993).

[251] Thanasegaran.

Special features and challenges

Malaysia is well known for its clear guidelines for halal (permitted) investment, as Bank Negara issues directives regularly on such investment. As a result, the participants of Islamic insurance as well as other Islamic investors, in Malaysia and abroad, can now invest in approximately 480 securities from the companies listed on the Kuala Lumpur Stock Exchange. Besides, Malaysian Islamic insurance participants have identified, with help from the government, other similar investments. For example, those insureds that have a life insurance policy with Syarikat Takaful Malaysia can invest the fund in their individual account to Bank Islam Malaysia for a period ranging from one month to over 60 months. This bank also helps this insurer lend its funds for special accounts to large corporations and individuals.[252]

Furthermore, the Malaysian government currently gives a tax relief of up to RM 5,000 for residents for their Takaful insurance premiums plus additional tax relief of RM 2, 000 specifically for such premiums for medical and educational purposes. As a result, 41,170 new life Takaful policies were issued in 1996 for coverage totaling RM 1.92 billion[253]. The total assets for life and non-life Takaful insurers in 1997 were approximately RM 300 million and RM 170 million, respectively.[254] During the same period, life Takaful insurance generated profits amounting to about RM 60 million and non-life Takaful gained about RM 40 million from the investment.

Malaysia Islamic insurance growth to soar beyond the expected growth rate is its competitive market structure of Islamic insurance industry. The rapid liberalization of Malaysia's Islamic financial industry has encouraged foreign institutions' participation in Malaysia, thus creating a diverse and growing community of domestic and international Islamic insurance operators. There are currently eight Islamic insurance operators and two Islamic re-insurance operators, with five foreign participations from the UK, Bahrain, Germany and Japan. This

[252] Obiyathulla Bacha, "Organizational Form and Efficiency: The Coexistence of Family Takaful and Life Insurance in Malaysia," *IDEAS Working Paper Series from RePEc* (2011).
[253]The Star, *Economic Report 96/97* (Kuala Lumpur: 1997), accessed 23 February 2018.
[254]Ramin Cooper Maysami, "Islamic Insurance: Sudan to Singapore," *Asian Business Law Review* 19, no. January (1998).

diversity of Islamic insurance operators helps in the reduction in the cost of doing insurance business.[255]

Moreover, Malaysian companies are considered to have higher re-insurance capacity even though they are less capitalized in relation to the amount of business managed by them. They use a smart investment strategy by giving priority to the liquidity of shareholders' fund investment portfolio, where the investment accounts represented almost 48% of total Malaysian shareholders' fund investment portfolio. Most investment accounts both in the GCC and in Malaysia are invested on a short-term basis. This is because the Islamic insurance operating companies perceive the investment accounts as the safest, easiest, and most liquid asset class available in the market. Although *Sukuk* (Islamic bonds) is a good alternative, the Takaful operating companies are reluctant to use this asset class to manage their liquidity due mainly to illiquidity of the Sukuk market. Globalization contributes to the development of vibrant Islamic insurance structure in Malaysia.

Despite its success, there are some lack of Islamic insurance development in some geographical areas and key market segment. The eastern states of Sabah and Sarawak have a very low Takaful penetration along. The study conducted in 2012 by Malaysia Takaful Association on Protection Gap showed that the low income, high cost, and challenges in product distribution contributed to the low Takaful and insurance penetration, in which made larger protection gap in these states.

Islamic insurance and other insurances in general are considered as not attractive among younger working population of age 30 and below. They are prioritizing their expenses on their immediate needs rather than long-term objective such as insurance or investment. It is noted that the key market segment with a large protection gap is attributed to those below age 30 years old who are largely single and are in the lower income group given that they would have only recently entered the workforce and would receive entry-level pay. This is consistent with the observations highlighted by the head of distribution channels of various Takaful operators interviewed in this study, whereby the younger generation are often reluctant and would delay purchasing insurance or Takaful protection cover. Furthermore, there has been low participation

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[255] Life Insurance International, "Takaful Insurance Booms in Malaysia," (May 2006), accessed 10 January 2018.

also from senior age population (50 and above). This is because the limitation on maximum age of entry and underwriting requirement. [256]The demand from low-income population has not been met with the suitable Islamic insurance product. Micro Islamic insurance products were identified as lacking in Malaysia. At this moment, the lack of product variety is also considered as one of the challenges for Islamic insurance development in Malaysia.

Altogether, the usage of very specific Islamic terms and contracts in Islamic insurance does not necessarily mean that there is new method invented in Malaysia. The method used is combination of several practices of Islamic financial contracts which is adapted to the existing conventional insurance regulatory framework in Malaysia. Companies have freedom to choose any method if the model does not breach Sharia principles. Their main goal of creating different methods of the application of Islamic insurance is to make the Islamic insurance business 'a profit-seeking commercial venture'. As a result, Malaysia has been contributing by 70% of the total regional market of Southeast Asia and 13% of the global market of Islamic insurance respectively.

Moreover, Malaysia has been developing Islamic insurance as a complete and diverse Islamic insurance service that is linked to other Islamic and non-Islamic financial services. These achievements are a result of a comprehensive institutionalization through public-private partnership scheme and sophisticated regulatory frameworks, with the government takes the major role in its development. Islamic insurance operation is regulated separately from the conventional insurance but still under mainstream mercantile law of civil court structure. It means Islamic insurance in Malaysia is not regulated under the Sharia court. Unlike other faith-based insurance schemes, The Takaful Act 1984 confined the operation of Islamic insurance within commercial or private sector. For this reason, Malaysia has become a model for many other countries to follow suit.

[256] MTA, "Protection Gap," MTA, accessed 5 January 2018.
http://www.malaysiantakaful.com.my/mta.optima.my/files/46/46f12fad-3d91-4c77-b638-7388055e1e4f.pdf

Making Islamic insurance 'national'

The 1979 revolution in Iran had an enormous global effect. It was for the first time the Islamist group gained power in a modern state. This event coincided with, and some have argued spurred, a wider resurgence of Islam around the world, including Malaysia.[257] There was an increasing demand for Islamization in Malaysia. There was growing popularity of the Islamist opposition political party Partai Al-Islam Se-Malaysia (PAS), *dakwah* (Islamic missionary) activities in Malaysia's schools and campuses, and demand for wider implementation for Sharia law.

Islamization process in Malaysia took various expressions; from a formulation that like a type of religious intolerance to the one that acceptable by different groups outside Muslim. Recently, the Arabic word for God, Allah, widely used by Arab and Indonesian Christians, is now reserved for Muslim use only.[258] On the other hand, Islamic finance is a kind of Islamization that is accepted by the public. One record shows almost half of the clients of Islamic finance are non-Muslim Malaysian. This section elaborates the coalition building behind Malaysia's Islamic insurance successes.

Also, the examination on Islamic insurance includes the assessment of Islamic finance infrastructure as a whole. As the Malaysian example shows the strength of *Bancatakaful* (combination of Islamic banking with Islamic insurance) has made Malaysia the second largest Islamic insurance market globally. There has been growth in Bancatakaful, and half of Family Takaful contributions come through this channel in Malaysia.

A window of opportunity

Shortly after Mahathir Mohamad was inaugurated as Prime Minister of Malaysia on July 16, 1981. He ordered the formation of a national steering committee to explore the possibility of opening an Islamic bank and Islamic insurance in Malaysia. There were three catalysts for this initiative. The first was the establishment of *Lembaga Tabung Haji* or Hajj pilgrim fund board by the government of Malaysia in 1963. Performing Hajj or pilgrimage to the Holy City of Mecca,

[257] Esposito, page 309–310.
[258] Lim Kit Siang, "Dap Supports Islamisation Based on the Constitution," *Malaysia Kini* (2 Spetember 2017), accessed 2 March 2018, https://www.malaysiakini.com/news/394035

Saudi Arabia is one of the pillars of Islam. Every Muslim supposed to do Hajj at least once in a lifetime. This ritual necessitates Muslims to devote enough financial resource to cover the expenses. Not all Muslims have enough financial means to do it immediately; therefore, most of them save some of their earnings until it is enough to cover the cost. Before Tabung Haji existed, Malaysian Muslims saved their money in conventional Banks.

Since the 1960s there had been a growing concern among Muslims in Malaysia related the use of conventional bank for saving their Hajj fund. The issue was on the use of interest by the banks and the un-Islamic way of banks' investment activities. Muslims of Malaysia demanded a financial institution that can facilitate their need to deposit their money for hajj and at the same time, avoiding the practice of interest which was considered as usury. Lembaga Tabung Haji was established to solve that problem. Currently, it is the only institution in Malaysia managing more than RM73billion of deposits (2017).[259] The success of Tabung Haji gave incentive for Mahathir's regime to expand the practice of Islamic finance in Malaysia. This institution was considered as the embryo of the Islamic bank in Malaysia. Until now, Tabung Haji has become the main source of investment for various Islamic financial institutions in Malaysia.

The second catalyst for the Islamization of finance is the development of Islamic bank in international level. The bank, so-called the Islamic Development Bank (IDB) was initiated by the Organization of Islamic Cooperation (OIC) with the purpose to generate financial cooperation among Muslim countries. IDB is working to improve the lives of those we serve by promoting social and economic development in Muslim countries and communities worldwide, delivering impact at scale.[260]Initially, OIC was established as a respond of an arson attack at Al-Aqsa mosque of Palestine. Global Islamic resurgence began in the 1970s with the Arab–Israeli war which triggered the global Oil Crisis in 1973. Events in the Middle East caused Muslims throughout the world to identify with the various plights of their co-religionists, particularly in the Palestinian issue. However, the member countries have tried to develop other meaningful cooperation beyond international politics. OIC is 2nd largest inter-governmental organization after the United Nation. It is "the collective voice of the Muslim world" and works to "safeguard and protect the

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[259] Lembaga Tabung Haji, "About Us," accessed 1 January, 2018. https://www.tabunghaji.gov.my/en/corporate/corporate-information/about-us#568.

[260] Islamic Development Bank, "Who We Are," accessed 18 February, 2018. https://www.isdb.org/who-we-are.

interests of the Muslim world in the spirit of promoting international peace and harmony".[261] IDB was established to serve these purposes through the vehicle of Islamic finance. Malaysia was one of the countries who was playing s prominent role in the establishment of OIC including ADB. Furthermore, the establishment of IDB provided an incentive for the creation of Islamic bank in national level including Malaysia. Tunku Abdul Rahman who was the Prime Minister of Malaysia before Mahathir was the committee chair of the establishment of IDB.

The third catalyst was the investment demand for the Petro dollar, mainly from Saudi Arabia. After the Oil boom in the 1970s, Saudi Arabia wanted to recycle their wealth and to assert its international influence by investing their Petro dollar to other Muslim majority countries. In order to capture this opportunity, Mahathir contemplated the possibility of Malaysia having a financial institution that capture this opportunity. They need an Islamic bank. In fact, it was Prince Mohamed Al Faisal of Saudi Arabia was the one who convinced Mahathir to open Malaysia market to an international Islamic bank. Due to legality issue, it was hard to establish an international Islamic bank in Malaysia at that time. Nevertheless, Malaysia already saw its importance and later, this has set the motion for Malaysia of building its Islamic banking system.

Beyond these three catalysts, the dynamics of national politics of under the secular regime of Mahathir was considered as the primary driver of Islamization of economy in Malaysia. Prior to Mahathir's accession to the premiership in 1982, UMNO had done little to co-opt Islam and Islamists into the umbrella of the Barisan Nasional (BN). According to Shamsul (1997), BN at the time was too busy dealing with internal political squabbles for such efforts to take precedence. Mahathir's prescription to meet the challenge of ABIM and PAS was to effectively redefine the debate between the two parties by embarking on a state-led, UMNO-led program of Islamization. Islamization was a representation of the religious conscience of the Malays. Although the global Islamic resurgence did serve to affect the religious conscience of the Muslim population in Malaysia, there are 'unique aspects to the resurgence of Islam in Malaysia that cannot be traced to the wider global dynamics'.[262] Unlike many Muslim countries, the promotion of Islamization in Malaysia was not an expression of growing disenchantment over the repressive

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[261] "About OIC," oic.org, accessed 9 September, 2018. https://www.oic-oci.org/page/?p_id=52&p_ref=26&lan=en.
[262] Jomo Kwame Sundaram and Ahmed Shabery Cheek, "The Politics of Malaysia's Islamic Resurgence," *Third World Quarterly* 10, no. 2 (1988): 843–868.

secular nationalism dictatorship and western domination of the relative underdevelopment of Muslim societies that led to the promotion of the possibilities of a better life under the auspices of an Islamic state. Under Barisan Nasional leadership, Malaysia was experiencing rapid economic development, coupled with the redistribution of wealth under the New Economic Policy (NEP), and meant that Malays were not in the same economic position as their Muslim brethren in the Middle East. Therefore, the domestic factors of Malaysia Islamic politics are more relevant in explaining the development of Islamic insurance in Malaysia.

In the 1980s, the common presumption that economic development was a secular project underwent a thorough reexamination in Malaysia. As a result, it created a demand to initiate a viable financial system: Islamic banking and Islamic insurance grounded in Islamic prescriptions. Indeed, there was a keen interest in Islamic finance across the Islamdom like Iran, Pakistan, and Sudan also sought to develop Islamic banking systems in the early 1980s.[263] At the same time, Malaysia had been facing high unemployment since the 1970s: the unemployment rate in the 1970 was 7.5%.

Nonetheless, Mahathir had been consistently voiced his rejection toward "western capitalist blueprints" for modernization. Therefore, he came up with plans—in part in response to Islamist political critiques—to design techniques for the provision of capital commensurable with both Islam and capitalism, but also guarantee autonomy against globalization as the ability of UMNO to distribute economic resources (as patronage) is the key to maintain its power.[264] The creation of a dual financial system and harmonization of Islamization with economic liberalization enabled Mahathir to build a political coalition to support the establishment of Islamic insurance in Malaysia. The first strategy has generated support from non-Malays to the project, and the second has produced continues approval and participation from the Malays population. Both policies are pursued as part of the adoption of the managerial role in the Islamic economy. As the manager, Malaysian state can incubate a new service economy in which private individuals and institutions (not the state) are the primary agents of economic growth.

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[263] Warde, page 114–125.
[264] Daromir Rudnyckyj, "Islamic Finance and the Afterlives of Development in Malaysia," *PoLAR: Political and Legal Anthropology Review* 37, no. 1 (2014): 69–88.

State as the manager of Islamic insurance

In June 1972, the National Fatwa Committee declared that the concept of conventional insurance contravened the rules of Sharia. Unlike those Iran, Pakistan, and Sudan, which sought the wholesale transformation of their banking systems into full-fledged Islamic systems, Malaysia "initiated Islamic banking in parallel with conventional banking on a trial basis".[265]In 1982, the Task Force to Study the Establishment of an Islamic Insurance Company in Malaysia was formed to look into the possibility of launching Islamic insurance as a complement to Islamic banking. Following the recommendations of the Task Force, the Malaysian Parliament enacted the Takaful Act 1984, thus giving birth to the Islamic insurance scheme in Malaysia that was entirely government driven and received full governmental support. Mahathir explains why it took that path, revealing that the systematic development of Malaysia's Islamic finance industry mirrors the administrative system the country was built on.

According to Mahathir: "When Malaysia became independent, we adopted the administrative system of the West. We adopted that, and we became familiar with having rules for everything. If you want to do something, you must have a law for it. Therefore, we had to provide a law for Islamic banking. Of course, the law was passed by parliament and not passed by some Islamic authority."[266] Creating the most comprehensive Islamic financial system in the world and this system operates parallel to the conventional interest-based system through a parliamentary framework gave national legitimacy for this initiative.

This systematic but pragmatic strategy created a much more conducive environment within a vulnerable inter-race relation of Malaysia. On the issue of multiracial Malaysia and Islamic finance, Mahathir says, "We have to be pragmatic. The world is not peopled by Muslims alone. Even in Malaysia, we have non-Muslims, and they have their rights too. We respect their rights. I told the non-Muslims that this [Islamic finance] is the Muslim way. They don't reject it. They even accept it."[267] The government set the goal of attaining a developed country status

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[265] Angelo M. Venardos, *Islamic Banking and Finance in South-East Asia: Its Development & Future, 3rd Ed.*, *Asia Pacific Business Series; V. 6* (Singapore; Hackensack, NJ: World Scientific, 2012), page 146.
[266] Emmy Abdul Alim, *Global Leaders in Islamic Finance Industry Milestones and Reflections* (Singapore Hoboken, New Jersey : Wiley, 2014).
[267] Alim.

before the year 2020. To this end, establishing a cordial partnership between Muslims and non-Muslims was essential in minimizing the political and socio-economic costs and risks inherent in unstable ethnic relationships.[268]

We can confirm this statement with the fact that there was no opposition on Islamic finance among the non-Malays including from DAP which was on the outside of Barisan Nasional coalition government. Lim Kit Siang, the DAP parliamentary leader, and Gelang Patah MP, once quoted the former ASEAN Secretary-General Surin Pitsuwan, to make a point that the Chinese-Malaysian population have no problem with Islamization. He said,” Surin said right up to the 80s, Islamization used to be a good word, where people integrated Islamic values and norms into every aspect of their life, including in education, work, and economic development. Furthermore, he said that DAP party supports Islamization based on the Malaysian Constitution, which promotes a nation-building process based on tolerance and mutual respect in a plural society and not one which engenders bigotry, hatred, and extremism.[269] DAP even agreed to cooperate with PAS particularly in 2008 when PAS was pursuing open, tolerant and inclusive policies under the leadership of Nik Aziz Nik Mat, Fadzil Noor and Yusof Rawa.

The affirmation of non-Malays group on Mahathir’s Islamization partly also because they were not able to form a strong opposition against BN. There has been a low level of non-Muslim (Chinese in particular) in this arena. It is generally assumed that the Chinese in Malaysia were not particularly concerned about Sharia-related issues, unless their interests were directly affected.[270] The non-Malays were too diverse to form a political coalition. For instance, the majority of Chinese and Indians were already co-opted under Barisan Nasional. The one outside the government such as DAP were left with two options of Islamization: the moderate and pro-capitalist version of Mahathir’s Islamization or PAS’ version of Islamic State. Although, once they cooperated with PAS against UMNO, in general, DAP preferred Islamization that carried by the government.

[268] Kikue Hamayotsu, "The Politics of Syariah Reform: The Making of Religio-Legal Apparatus in Malaysia," in *Malaysia: Islam, Society and Politics*, ed. Virginia Hooker and Norani Othman (Singapore: ISEAS, 2003)., page 68.
[269] Siang.
[270] Hamayotsu, "The Politics of Syariah Reform: The Making of Religio-Legal Apparatus in Malaysia," in *Malaysia: Islam, Society and Politics*.

Based on its center-left platform, DAP prefers to have more government involvement in health care and public service. Nonetheless, DAP stresses the need for government to run efficiently. In the issue of 1Care, a reform plan that would give universal healthcare for Malaysia in 2012, DAP showed criticism in term of how this program could be supported financially. Lim Kit Siang stated," Healthcare is a human right and each and every government of this world is obliged to provide to its citizens the best of healthcare in the form that is most efficient, cost effective and acceptable to its citizens."[271] In summary, the development of Islamic insurance through a dual system has not been considered as a threat for the well-being of the Malaysian minority, particularly compared to the previous economic program of NEP which certainly bias toward Malays. They also accept Islamic insurance if it is developed as private-based insurance that does not give a financial burden to the state and does not disrupt the existing business environment.

From the perspective of UMNO leadership itself, support from the Chinese in Malaysia particularly the Chinese corporate figures are important. The recession in the later 1980s exposed the fundamental weakness of Bumiputera entrepreneurs. Mahathir found that vibrant Chinese capital, together with the energetic Chinese workforce, was a vital asset to the Malaysian economy. This fact became an incentive for Mahathir to ensure Islamic finance project that entertains Chinese interest and demands. The UMNO government could not afford to have the Chinese community in general, and Chinese capital in particular, lose confidence in its leadership. The dual system did not pose a serious threat to Chinese and corporate business in general. The Islamic finance law was introduced without replacing paralleling laws on the civil side and the administration of these laws remained under the jurisdiction of civil courts. Therefore, they welcomed this system and supported UMNO political agenda if Malaysia's liberal business practices were kept untouched.

Furthermore, there are many non-Muslim Malaysians participants in Islamic finance, particularly Islamic insurance. A study by Swartz and Coetzer mentions that Islamic insurance

[271] John Teo, "1 Care: Show Us the Mathematics," *The Malaysian Insider* (19 February 2012), accessed 18 April 2018, https://blog.limkitsiang.com/2012/02/19/1-care-show-us-the-mathematics/.

products have attracted even non-Muslim communities.[272]Although no hard numbers are available, the industry has trumpeted the non-Muslim take-up rate for Islamic banking products over the years. It is well-known in the financial sector that most customers of the country's fully-fledged Islamic banks-such as Bank Islam Malaysia and Bank Muamalat-as well as the Islamic banking "windows" of conventional banks, including Maybank, Public Bank, HSBC, Citibank and Standard Chartered-are, in fact, non-Muslim. A report released by PricewaterhouseCoopers in 2008 claimed that more than 50 percent of Islamic banking customers are non-Muslim.[273]

Although it was designed as an alternative political and economic framework using specific Islamic terms and contracts, Islamic insurance and Islamic finance, in general, are very inclusive for various players. In 1993, the central bank introduced the Interest-Free Banking Scheme.[274] This program offered tax breaks for conventional banks that opened Islamic “windows” to offer Islamic financial products, such as home mortgages or savings accounts. Similarly, conventional banks could use their existing institutions and infrastructure to expand into Islamic banking and Islamic insurance on a gradual basis and offer conventional and Islamic financing options under the same umbrella. According to some observers, the Islamic window scheme offered the most cost-effective and efficient way to “disseminate Islamic banking on a nation-wide basis, with as many players as possible, so as to be able to reach all Malaysians”[275], and which allowed Malaysia to quickly grow its Islamic financial sector. Furthermore, by increasing the number of firms in the sector, the state spurred the innovation of instruments and products.

To further facilitate the growth of Islamic insurance, the Malaysian government had increasingly built a network of Islamic financial institutions rather than relying on a single state-supported Islamic insurance company. Foreign insurance companies have been active in acquiring stakes in local insurers through mergers and acquisitions (M&A) since 2010. Between 2010 and 2016, the Malaysian insurance industry saw the conclusion of around 20 M&A deals valued at about RM16bn, notably in the more fragmented general insurance segment. The

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[272] Nico P. Swartz and Pieter Coetzer, "Takaful: An Islamic Insurance Instrument," *Journal of Development and Agricultural Economics* 2, no. 10 (2010).
[273] Alim, *Global Leaders in Islamic Finance Industry Milestones and Reflections*.
[274] Munawar Iqbal and Philip Molyneux, *Thirty Years of Islamic Banking* (2005).46
[275]Rudnyckyj, “Islamic Finance and the Afterlives of Development in Malaysia.”

industry's consolidation and the entry of global players resulted in larger and stronger insurers, as well as greater sophistication for the domestic industry through product innovation, pricing and risk-management expertise as well as multi-channel, including digital, distribution.

At this moment, AIA and Great Eastern are dominant players in the domestic life insurance segment landscape, cumulatively commanding close to 50% of market share by net premium contribution. AIA, Great Eastern and Zurich have Islamic product offerings. While AIA and Great Eastern each has a local partner for the Takaful JV (Public Bank and *Koperasi Angkatan Tentera* respectively), Zurich's operations are wholly owned. In 2006, Hong Leong Bank - the sixth-largest local bank entered the Islamic insurance market.

Abdullah Ahmad Badawi, prime minister from 2003 to 2009, continued the policies inherited from Mahathir Mohamad. Abdullah persisted with a developmentalist model that promoted Bumiputera capital, but he showed little interest in developing Malay – or Malaysian – big businesses. He nurtured SMEs, including cottage industries dealing with halal products, dominated by poor rural Malays, as well as Islamic-based financial services as he believed firms in these sectors had export capacity potential if developed well. Since the 2005 census of the corporate area revealed that SMEs constituted about 99.2 percent of all business establishments, this new effort to establish these firms was an astute economic – and political – move. SMEs then employed 5.6 million workers and contributed about 32 percent of real GDP. Eighty-seven percent of SMEs are in the services sector, 7.2 percent in manufacturing and 6.2 percent in agriculture. Ninety-nine percent of firms in agriculture are SMEs. Key sub-sectors within services comprise those related to Islamic financial products, including banking and Islamic insurance.[276]

Altogether, the state has limit itself on the role of an incubator or manager for Islamic insurance rather than as a direct participant. The Malaysian state created the necessary infrastructure to facilitate the emergence of viable national and transnational Islamic financial systems but did not become involved in creating commercial firms. The key institutions developed by the state include special offices within the Bank Negara Malaysia; research and educational institutions; and the Islamic Financial Services Board (IFSB), which is an international standard-setting organization that develops global standards and guiding principles for Islamic

[276] See Malaysia (2006: 166-67) for further details about public programs to aid SME development.

financial institutions. The state's effort to act as an incubator rather than as an agent of Islamic finance is further evident in its insistence that the Islamic sector competes with the conventional sector.[277] Compared to the affirmative policy of NEP of the 1970s, the creation of a dual financial system has been seen as more inclusive and non-discriminative against non-Malays population. The dual system model offered the opportunity to maintain order in the conventional system, generating political support while simultaneously incubating the embryonic Islamic system.

Harmonizing Islamization with economic liberalization

Malaysian government provides more support –particularly in comparison to Indonesia and Pakistan- in the establishment of the private-based Islamic insurance of Takaful. The next question would be: If Islamization is a tool for the Mahathir regime to gain public support and legitimation, why he pursued an Islamic but private-based insurance model rather than using populist policy. For example, he could rely on expanding social insurance by utilizing Islamic instrument such as zakat (religious tax). Creating Islamic social insurance seems to be the most rational option, mainly when there is less disagreement among the scholars of Islam on the permissibility of social insurance.[278] Mahathir could get Muslim support and at the same time, there was no need to devote more resources from public funding.

There were budgetary deficits highlighted the economic vulnerability in the mid-1980s, partly due to the large size of the public sector. Therefore, to overcome the crisis and build a stronger foundation for the economy, it was decided that Malaysia needed more economic liberalization and deregulation and that the private sector should be the engine of growth. Liberalization would introduce more competition, attract foreign capital and increase efficiency. So, how the Mahathir government could gain support from the Malay population for his economic liberalization agenda? Islamic insurance has a prominent role in this process. Therefore, Malaysia as s state needed to take command on the Islamic finance agenda.

Mahathir understands the Islamdom is not a monolithic *homo Islamicus*. In his memoirs, he writes about Muslims' different interpretations of Islamic principles and injunctions that lead

[277] Rudnyckyj, "Islamic Finance and the Afterlives of Development in Malaysia."
[278] Alim, *Global Leaders in Islamic Finance Industry Milestones and Reflections*.

to factions. Therefore, a centralized body for the Islamic finance industry was needed to create a uniform model for an assemblage of religious and economic practices, which are two domains that earlier efforts toward secular modernization had presumed separate. This centralized Sharia body developed concepts and methods of Islamic finance that both represented Islamic values but also serves the goal for economic liberalization of Malaysia.

The variation in policy responses of the countries stems from difference in the preferences of regime supporters over the idea of Islamization in general, and particularly Islamization of insurance. In Malaysia case, the establishment of Islamic insurance was tied up to a broader privatization project envisioned by Mahathir including privatization of Malaysia's health care, social security and Malaysia economy in general. While in previous decades, the Malaysian Government had prided itself on its achievements in health care and the welfare model of federal health care services, under the Mahathir administration the public health care sector was increasingly regarded as a burden, which the government would be unable to carry in the future. The government's concept of Vision 2020, with the goal of Malaysia reaching developed country status by the year 2020, has eschewed the welfare state.

Prime Minister Mahathir has asserted the need for "a social system in which society will come before which the welfare of the people will not revolve around the state or the individual but around a strong and resilient family system". Several schemes for financing health care have been articulated by the government. These include the use of compulsory savings, private insurance, and employer-funded private coverage.[279] At the same time, the success of affirmative action of the New Economic Program since the 1970s in creating a Melayu *Baru* or the new Malay elite society encouraged the creation of protection system which both Islamic but also economically sound. Malaysia's health care system required a significant growth in the private health care sector, a high proportion of health care expenditure comes from out-of-pocket, to sustain high quality and high cost of medical technology.

There had been demographic changes to the UMNO voters. UMNO traditionally gained support from Malay community and peasants in the villages. However, more Malays migrated to

[279] Simon Barraclough, "Constraints on the Retreat from a Welfare-Orientated Approach to Public Health Care in Malaysia 1 This Article Is a Revised Version of a Paper Delivered at the Twelfth New Zealand International Conference on Asian Studies, Massey University, 26–29 November 1997. 1," *Health Policy* 47, no. 1 (1999): 53–67.

cities, worked in a corporate environment, and gained a college degree. This transformation of the voter characteristics from rural agricultural to more urban Muslim encouraged UMNO to introduce a program that appealing from them. Most of them were not the poor who need charity from zakat, but they were more interested in job and business opportunities. The characteristics of Islamic finance in Malaysia were designed for this particular urban entrepreneurial group. Furthermore, Islamic insurance is an idiom that capture this transformation.

Both Mahathir Mohamad top-down state-directed initiatives and bottom-up societal pressures played a significant role in this process. The three-decade regime managed to create a coalition between the urban, modern, and middle-class Malay Muslim population and Malay entrepreneur in building private-based Islamic finance. At the same time, there has been a continued and continuous pressures from the *dakwah* movement (Islamic missionary) of *Angkatan Belia Islam Malaysia* (ABIM) or the Muslim Youth Movement of Malaysia.

Mahathir had been careful enough to limit the role of the traditional religious council (the older *ulama*) as merely supporter and far from being the driver of the Islamization. Developing Islamic instrument through private scheme serves both strengthening the Malaysian Muslim bourgeoisie or entrepreneur class and facilitate Mahathir's broad economic developmental goals, which would further add to UMNO's popularity and electoral legitimacy but without jeopardizing the authoritarian and capitalist structure of Malaysia. Islamic insurance development in Malaysia reflects a continued and continuous dynamic interaction of both processes: top-down state-directed initiatives and bottom-up societal pressures, especially from the *dakwah* movement of ABIM.[280]

The establishment of Islamic insurance was intended to take the momentum of public positive response toward the establishment of *Bank Islam* one year before and to capture the emerging market of the new urban and modern Malay Muslims as a result of the successful affirmative action of NEP. The success of Bank Islam had provided a pathway for the establishment of Takaful. Syarikat Takaful started operations in August 1985 with a paid-up capital of RM10 million. Bank Islam was its majority shareholder, with others being state religious

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[280] Abbott and Gregorios-Pippas.

councils and state religious development agencies. In its first year of operations, Syarikat Takaful attracted 6,000 Takaful participants, with the number rising to 50,000 by the end of May 1987. In fact, Tan Sri Nor Mohamed Yakcop, who was responsible for the implementation of Islamic banking at Bank Negara Malaysia until the early 1990s, explains," We agreed from Day 1 that we would establish, over period of time, an entire ecosystem of Islamic finance consisting of banking system, a capital market, stock-broking, and Takaful (Islamic insurance)." [281]

Before the 1980s, Malaysia had proceeded the presumption of a de facto separation of religion from the economy. Malaysia's initial development success stemmed from its position in the 1970s and 1980s as a global center for high-tech assembly and offshore industrialization.[282] With the active encouragement of the developmentalist state, firms from Europe, Japan, and the United States set up shop in large industrial zones and hired a vast number of workers to provide the labor for export-oriented growth.

Although economic modernization was primarily a secular project, the state took a special interest in the economic standing of the Bumiputera. This concern accelerated after the widespread ethnic riots in 1969. These efforts became particularly pronounced in the state's New Economic Policy (NEP), which was initiated in the 1970s. The policies provided ethnic Malays, who were by state definition Muslim, with privileged access to state benefits such as civil service positions, state-held trusts, business licenses, government contracts, and preferential access to higher education in the national university system. Secular economic development saw the rise in the fortunes of the elites, Melayu Baru (the New Malays).

By the 1980s, the common presumption that economic development was a secular project underwent a thorough reexamination in Malaysia. Indeed, this secular economic development helped to improve the economic condition of Bumiputera. Nevertheless, it also accelerated the rise of Islamism in Malaysia, especially in the universities. Moreover, these university students especially have increased their involvement with campus *dakwah* organizations, which gave rise to the moderate Islamist movement of ABIM.

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[281] Alim, *Global Leaders in Islamic Finance Industry Milestones and Reflections*. page 112.
[282] Aihwa Ong, *Spirits of Resistance and Capitalist Discipline Factory Women in Malaysia* (Albany: State University of New York Press, 1987).

There were also some unintended consequences. The rise in the fortunes of the elites, many of whom were politically connected; and their ostentatious displays of wealth and conspicuous consumption became a focus of criticisms by Islamists who viewed newly rich Malays as morally suspect, inattentive to Islam, and "corrupt and greedy.[283] There has been growing dissatisfaction toward the government that was considered as un-Islamic. There were demands represented by ABIM and PAS that Islam should not be merely instrumental terms but as a comprehensive system of values that should encompass all spheres of human activity.

When the modernist Mahathir came to power in 1981, Islamism became the most effective ideological weapon against the UMNO. After decades of removing the threat from the political left, Islamist has become the primary opponent of the ruling power. Rather than removing the threat forcefully, the UMNO-led government responded to this Islamic revival by supporting the social policy of Islamization. UMNO assume Islamic veneer and to incorporate varying Islamic elements in its program. The cooptation of a charismatic and visionary leader of ABIM, Anwar Ibrahim, marked the vital point of the Islamization process in Malaysia.

Prior to Mahathir's accession to the premiership in 1982, UMNO had done little to co-opt Islam and Islamists into the umbrella of the Barisan Nasional. According to Shamsul, the Barisan at the time was too busy dealing with internal political squabbles for such efforts to take precedence. Mahathir's prescription to meet the challenge of ABIM and PAS was to effectively redefine the debate between the two parties by embarking on a state-led, UMNO-led program of Islamization. To give credence to this, nine months later Mahathir spectacularly brought Anwar into UMNO's fold and 'with Anwar's help, Mahathir was able to quickly formulate new Islamic policies that were received with wide approval from the country's ulama or the clergy. Anwar's co-option was all the more spectacular since many within PAS had anticipated that Anwar would become its leader in the future.[284]

It is clear that Anwar's co-option signaled the beginning of the institutionalization of Islamization within the bureaucracy. The first initiative was the introduction of '*Penerapan Nilai-nilai Islam'* which was 'a policy guideline for the incorporation of Islamic ethics in governance'.

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[283] Chandra Muzaffar, *Freedom in Fetters: An Analysis of the State of Democracy in Malaysia* (Aliran Kesedaran Negara, 1986), page 70.

[284] John L Esposito, *Islam and Democracy [Electronic Resource]* (New York: Oxford University Press, 1996).

This policy led to the establishment of an Islamic Consultative Body, the Institute for Islamic Understanding, and the IIUM in 1983, and an Islamic Development Foundation in 1985, as well as an Islamic insurance company and an Islamic bank (Bank Islam Malaysia Berhad) in 1984.[285]

Another important development was the introduction of *Pusat Islam* which in effect was a 'government sponsored Dakwah group, intended to compete with other Dakwah movements and to report on their activities'. Over time Pusat Islam would grow into a fully -fledged department of government known by the acronym JAKIM (Jabatan Kemajuan Agama Islam Malaysia – Department of Islamic Advancement of Malaysia). Additionally, to ensure Malays were educated about UMNO's 'progressive' approach to Islam (as opposed to PAS's version of Islam), the government sanctioned policies that saw an increase in Islamic programs over the radio and television.

Some members of ABIM rose up to become what so called urban ulama. They have a background in Islamic studies and well-versed in Islamic law, but unlike traditional ulama, they have influence beyond their particular village or *kariah*. They are professors in universities, live in cities, speak in international forum and media, and address contemporary social issues. These ulama were recruited by the state to build Malaysia Islamic finance. They are the epistemic community behind Islamic finance. They sit together with bankers, actuaries, and bureaucrats to formulate regulations on Islamic finance. The emergence of urban ulama is, in part, precipitated by an alliance between state elites and Sharia bureaucrats in cities, particularly Kuala Lumpur, as Sharia professionals have been placed on state as well as Islamic Finance Institutions' payrolls. Sharia professionals in these institutions and government administration are rewarded with higher salaries, power, status, and mobility, especially those recruited to federal agencies in charge of administering Sharia compliance. They are more cosmopolitan than their rural counterparts actively codifying legal discourses and engaging in Islamic legal theorization.[286] Furthermore, these Sharia experts were interested non-only in upgrading their socio-economic

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[285] Abbott and Gregorios-Pippas.

[286] Jessie P. H. Poon, Jane Pollard, and Yew Wah Chow, "Resetting Neoliberal Values: Lawmaking in Malaysia's Islamic Finance," *Annals of the American Association of Geographers* 108, no. 5 (2018).

status but also in maximizing their jurisdictional boundaries.[287] At this moment, this group of urban ulama is known as 'Islamic business developer' or 'entrepreneur'.

Without questioning Mahathir's own religious convictions his decision to bring in Anwar was clearly a calculated and strategic decision brought in to deliver the Islamic votes to UMNO'. However, Mahathir was not only motivated by the desire to blunt the appeal of ABIM and the influence of the Dakwah educated students. Analyzing his key policy pronouncements, it is clear that Mahathir hoped to utilize Islam as a vehicle to facilitate his broad economic developmental goals, which would further add to UMNO's popularity and electoral legitimacy. Mahathir's vision of Islam was one that he believed could be harnessed to UMNO's original goals of nationalism and capitalism.

The Islamist party of PAS has been supportive toward the development of Islamic finance in Malaysia, but they have been very critical in the way Mahathir's operated it by neglecting poor people. Although PAS always promote the responsibility of the state to take care of its citizen including providing free health care, PAS has no principle disagreement on the concept and the practice of Islamic insurance. PAS even has been developing its own Islamic insurance schemes for PAS member (Takaful Kifalah dan Takaful Armalah). PAS had objection on the way government pursued the development of private insurance by reducing its public funding especially in health care. Mahathir's Islamization along with privatization and deregulation program have left behind pools of poverty, urban and rural, while only a small group of elite Malays have become much better off. According to PAS leader, "PAS shall continue to assess and address the impact of globalization, in so far as it affects the development of a better Malaysia and a better world." Rather than a piecemeal program offered by BN, PAS claim that Islamic State would solve the problem. Although PAS was known as the defender of the people, its Islamic State idea has never been expressed clearly, compared to the one proposed by BN and Mahathir. Moreover, Mahathir has accused PAS of misrepresented Islam by promoting terrorism, conservatism, fanaticism, backwardness, poverty, and degrading stereotypes."[288] PAS was hardly

[287] Hamayotsu, "The Politics of Syariah Reform: The Making of Religio-Legal Apparatus in Malaysia," in *Malaysia: Islam, Society and Politics…,* page 75.
[288] Amrita Malhi, "Pas-Bn Conflict in 1990," in *Malaysia: Islam, Society and Politics*, ed. Virginia Hooker and Norani Othman (Singapore: ISEAS, 2003).

able to compete with BN in winning Malay/Muslim voters, particularly after Mahathir successfully coopted Anwar Ibrahim into his government.

Furthermore, the state conducts some regulatory reforms to reduce the ambiguity in Islamic finance. The state reduced uncertainty in Islamic finance by reducing conflicts over interpretations of Islamic law. Politically, this has been substantial in solidifying support for the Mahathir's Islamization project. For instance, The Central Bank of Malaysia Act, passed in 2009, contained key provisions regarding the status of the National Sharia Advisory Council or NSAC. These provisions effectively administered compliance with Islamic prescriptions by granting the NSAC the status of the sole authoritative body on Sharia matters about Islamic banking, Islamic insurance, and Islamic finance. The act itself granted the NSAC the power to prevail over any other ruling passed by a Sharia body in Malaysia, and it stipulated that any courts or arbitrators were required to refer to NSAC rulings in any dispute pertaining to Islamic financial business. Finally, it mandated that any rulings of the NSAC were binding. This essentially gave the NSAC supreme authority in the arbitration of matters connected to Islamic finance. Rudnyckyj argues, "Efforts to rationalize interpretations of Sharia reveal an important aspect of the afterlife of development: the production of new types of knowledge requires intervention to ensure that systems operate consistently and predictably. In this instance, the state ensured the efficient functioning of the Islamic finance infrastructure by mitigating the potential for conflicting interpretations of religious injunctions."[289]

The establishment of the strategic investment fund of the Government of Malaysia, Khazanah Nasional Berhad, is to help to maintain economic autonomy and strengthen capital expansion. Khazanah is entrusted to hold and manage the commercial assets of the Government and to undertake strategic investments on behalf of the nation. It is a novel way to strengthening Bumiputera capital ownership in a certain way. This company also acts as re-Takaful company. The world's largest Islamic re-insurance company are ACR ReTakaful Holdings Ltd, owned by ACR Capital Holdings, the Dubai Group and Malaysian sovereign wealth fund Khazanah Nasional Bhd,

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[289] Rudnyckyj, "Islamic Finance and the Afterlives of Development in Malaysia."

with a paid-up capital of $300 million, according to its website.[290] Mahathir Mohamad founded the sovereign wealth fund, Khazanah, in 1994.

Khazanah's portfolio features some of Malaysia's most significant and most strategic listed entities, such as telecommunications giant Telekom Malaysia and its regional mobile operator Axiata Group, financial powerhouse CIMB Group Holdings, national power utility Tenaga Nasional, airports operator Malaysia Airports Holdings and IHH Healthcare. Khazanah is also the sole shareholder of the country's financially troubled national air carrier, Malaysia Airlines. In Singapore, Khazanah and Temasek are joint-venture partners in M+S Pte Ltd, which is involved in the development of four parcels of land in Marina South and two land parcels in Ophir-Rochor on which Marina One and Duo now stand. It is stated in the website,

> Khazanah’s portfolio cuts across various sectors and industries. Our companies comprise some of the most significant companies in Malaysia, as measured by their strategic importance to the nation. They include Government-Linked Companies (GLCs) in sectors such as aviation, financial services, power and telecommunications. We also invest in new sectors and geographies to support the transformation of the Malaysian economy. Via these investments, we hope to build new industry linkages and help boost national growth and development.[291]

Beyond this purpose, this company had been used as a convenient vehicle for the government to reward politicians and non-professionals with positions and lucrative compensation packages.[292]

Although the government of Malaysia does not involve directly in establishing Islamic finance companies, the success of Islamic financial institutions is very much dependent on deposits of government money, rooted in a rent-based model just as NEP-era businesses had

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[290] Liau Y-Sing, "Malaysian Body Creates New Islamic Reinsurance Model," (18 March 2010), accessed 5 January 2019, https://www.reuters.com/article/us-islamic-financial-retakaful/malaysian-body-creates-new-islamic-reinsurance-model-idUSTRE62H2F420100318.

[291]khazanah.com, "Our Investment," accessed 10 February, 2019. http://www.khazanah.com.my/Our-Investments/Sectors#.

[292] Leslie Lopez, "Malaysian Sovereign Wealth Fund Khazanah's Directors Resign after Pm Mahathir's Criticism," (26 July 2019 2018), accessed 15 March 2019, https://www.straitstimes.com/asia/se-asia/khazanahs-directors-resign-after-mahathirs-criticism.

been.[293] The government and its subsidiary companies are the primary investors in Malaysia's massive Sukuk issuances. Zakat contributions make up a hefty segment of money on hand in Malaysian Islamic banks. The Employee Provident Fund – Malaysia's pension system – often invests its money in Islamic instruments. Think tanks such as INCEIF and ISRA, conferences held in Kuala Lumpur, and global promotion and marketing are largely funded by Bank Negara and the state.[294]

Islamic finance and Islamic insurance serve as meeting point for diverse political interests. For Mahathir, UMNO and BN, Islamic finance mitigates the real threat posed by Islamism. Dakwah movement of ABIM and Islamists political party of PAS were pushing demand of having Islam as a comprehensive system of values within Malaysia polity. To gain support from Malays population and present the UMNO government as Islamic, Mahathir responded by supporting the social policy of Islamization. Moreover, Mahathir reshaped this Islamization process by co-opting the leaders of ABIM, especially Anwar Ibrahim, and directed the Islamization project. On economic matters, Mahathir reshaped Islamization agenda by creating Islamic finance in a way that harmonious with his economic development agenda.

Moreover, Islamic insurance prepared the transformation toward a social system based on a strong and resilient family system. Mahathir has been keen to exploit the dynamism of market forces to shake up the bureaucracy and Malay values. On the other hand, the mechanism that might transform Malay values - market forces - and help make the Bumiputera more "authentic" capitalists and less dependent on either state assistance or politically strategic relationships with Chinese businesspeople. Mahathir sought to exploit what he takes to be the beneficial, transformative effects of market forces without sacrificing government control or oversight. [295] For Malay population, Islamic insurance presents an idea that Malays can be modern but still maintain their uniqueness, but for UMNO it was a tool to enter globalization that provides control over its patronage relationship with the domestic corporate figures. The goal for

[293] Edmund Terence Gomez, Johan Saravanamuttu, and Maznah Mohamad, *The New Economic Policy in Malaysia: Affirmative Action, Ethnic Inequalities and Social Justice* (Singapore: NUS Press, 2013).
[294] Sloane-White.

[295] Mark Beeson, "Mahathir and the Markets: Globalisation and the Pursuit of Economic Autonomy in Malaysia," *Pacific Affairs* 73 (2000): 335–51.

autonomy from globalization was the main reason behind his rhetoric against western capitalism blueprint.

Islamic insurance received support from a broad political coalition. For the ruling government of Barisan Nasional and private sectors, Islamic insurance has been one of the tools to harmonized Islamization and economic liberalization. It was an avenue for the maintenance of the UMNO's dominant political position, as this is still dependent on its ability to control and distribute economic resources. Meanwhile, ABIM and PAS support this alternative insurance because it is imbued by Islamic values and present the 'more Islamic' picture of Malaysia. Moreover, it was also an alternative avenue for *Bumiputera* capital growth, job entry to the government, and opportunity for expansion of Sharia jurisdictions. At the same time, there was no strong opposition against Islamic insurance from non-Malays including the center-left party of DAP, insurance businesses and corporate figures because Islamic insurance is a private-based scheme thus it is considered as more efficient in term of public funding. Furthermore, its establishment did threaten the existing liberal-capitalistic business environment, on the contrary, Islamic insurance expanded this system and provided benefits and more opportunities for them. Islamic insurance is a deal between the need for Islamic values, liberalization agenda, and need for economic autonomy.

Malaysia's *Barisan Nasional* coalition depended on (continues to depend on) an alliance between the Malay masses and a class of Malay entrepreneurs. Favoritism in economic and social policy ensures support from ordinary Malays; favoritism in corporate and financial policy ties the new Malay rich to the regime. The strategic use of ethnicity is the key to continual maintenance of this system of exchange and support across classes, for it demonstrates how regime institutions embedded each group's economic interests directly into the system of rule. The new coalitional alignments between ordinary Malays and the new Malay rich, pressure from the "fundamentalists" PAS, weak opposition from Chinese Malaysian community, and support from corporate actors are instrumental for understanding the development of Islamic insurance in Malaysia.

Adding to that, the success of Islamic insurance in Malaysia post-Asia financial crisis can also be attributed to the continuing authoritarian system of Malaysia's polity. Mahathir

maintained political dominance meaning there had been no changes in the Islamic finance structure. There was less transaction cost due to political readjustment compared to the democratization of Indonesia by the end of the 1990s. There had been no serious challenge toward the regime during that time and its institutions. The Islamization project that initiated from the center of political power was left untouched.

Corporate Islam and the acceptance of Islamic insurance

Insurance markets in Muslim countries are mainly at nascent or growth stage of development with a very low insurance density, even in the most developed Muslim nations. Based on a comprehensive study by Feyen, Lester, Rocha the reasons are the religious prohibitions, underdeveloped financial systems, weak contract enforcement, consumer skepticism, corruption, lack of understanding of the benefits and necessity of insurance, limited technical expertise and low GDP per capita. [296] So, how Islamic insurance has become accepted in Malaysia society in a relatively short time?

Indeed, the improvement of those variables mentioned by the study above influenced the development of Islamic insurance in Malaysia. Because of the New Economic Policy (NEP) of May 1969, Malays have become wealthier and taken greater control over Malaysia's economic resources. The steady development with government support of Islamic finance since the 1980s also increased consumer trust toward Islamic Finance institutions. Nonetheless, understanding the interaction between those variables, particularly the role of religion and Malay's culture helps us to have a more profound understanding of this development.

This section discusses the 'social life of Islamic insurance' meaning how Islamic insurance as a commodity has become accepted as a social practice within Malays society. It elaborates the redefinitions of Islamic economic beliefs and meanings that have shaped the Malay understanding of entrepreneurship and human agency. Patricia Sloane-White argues that the development of Islamic finance is not only creating a new class of Malay entrepreneurs but also transforming Islamic values. She suggests, "Sharia principles at play in Malay-Muslim economic

[296] Feyen.

life do not merely produce Islamically regulated things, but produce and emplace Islamic norms, ethics, hierarchies, practices, and gendered identities enacted in corporate life. That is, they produce Islam."[297]

This section consists of two parts. The first part explains how Malay society reset market values inherent in the Islamic insurance to be in line with their Islamic values and the second part contains discussion on the emergence of Malay entrepreneurship. This first part focuses on how Malaysians consume, rework, and accept Islamic insurance, whereas, the evolution of Malays entrepreneurship plays the most crucial role in it. The second part provides a historical explanation on how the affirmative policy of NEP and the subsequent Islamization during Mahathir created a new class of entrepreneurial Malays. This class is not only different from other groups in term of socio-demographic characteristics but also in mindset. Sloane uses the term 'Corporate Islam' to describe the middle-class urban Malays who are using entrepreneurship not only as an occupation but also identity. This identity is integral with their understanding of being a Malay, Muslim and modern. Islam is reconfigured as an ethical and entrepreneurial religion. This 'altered' identity provides susceptible ground for novel schemes of Islamic finance including Islamic insurance to develop and to be accepted.

Islamic insurance as an idiom for self-reliant, piety and care responsibility

Many studies have been conducted to understand the relationship between entrepreneurship and insurance. The findings show how insurance encourages entrepreneurship because insurance creates more predictability and manages business risk. The risk-averse businesspeople will likely to invest in new business ventures as insurance will overcome a possible loss. [298] Many of similar study assume there is singular understanding on insurance. However, the concepts of risk, risk sharing, distributive justice, generalized reciprocity, and hedging against financial catastrophe are understood and addressed in relation to the values or culture in local worlds. Insurance as both a concept and an institution have been presented to

[297] Sloane-White.
[298] Pietro Masci, "Insurance and Entrepreneurship: A Conceptual Framework," *Journal of the Washington Institute of China Studies* 7, no. 1 (2012).

the public in various ways by different stakeholders. Public perceptions of and demand for insurance are not static. They are sensitive to changing policy, practice, experience, and flows of information.[299] Golomski argues, "Like biomedicine or finance, insurance tends to travel globally as a culture-free form of knowledge," but then he adds, "Recent ethnographic research shows how insurance is consumed, reworked or rejected in novel ways."[300] Insurance does not have a single meaning, logic, or effect but needs to be viewed in practice, in context, and from multiple vantage points.[301] This part of this chapter focuses on how Malaysians consume, rework, and accept Islamic insurance, whereas, the evolution of Malays entrepreneurship plays the most important element in it.

The price of premium and services of Islamic insurance are not entirely different from conventional insurance. Islamic insurance companies and brokers were *ethnopreneurial* in their marketing by using language and symbols of ethnic or religious identity. This research founds five symbols that are presented in the introduction of Islamic insurance in Malaysia:

1. Islamic insurance as care responsibility toward a family.
2. Islamic insurance is Islamic.
3. Islamic insurance embodies cooperation/risk sharing
4. Islamic insurance is operated by for-profit companies.
5. Islamic insurance is supported by the government.

In order to understand the social life of Islamic insurance, we examine five aspects of Islamic insurance in Malaysia. I use secondary sources that documented interviews with people who buy Islamic insurance, particularly from the qualitative study conducted by Naail Mohammed Kamila and Norsham Binti Mat Norb.[302]

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[299] Dao and Mulligan, "Toward an Anthropology of Insurance and Health Reform: An Introduction to the Special Issue."

[300] Casey Golomski, "Crisis, Risk, Control: Anthropologies of Insurance. In Focus," *Anthropology News*, 54 (2013), https://www.academia.edu/5061446/Crisis_Risk_Control_Anthropologies_of_Insurance._In_Focus._Anthropology_News_54_9-10_10-11.

[301] Dao and Mulligan, "Toward an Anthropology of Insurance and Health Reform: An Introduction to the Special Issue."

[302] Naail Mohammed Kamil and Norsham Binti Mat Nor, "Factors Influencing the Choice of Takaful over Conventional Insurance: The Case of Malaysia," *Journal of Islamic Finance* 3, no. 2 (2014).

The Family Takaful sector in Malaysia is noted to make up the more substantial portion of the Islamic insurance operators' business portfolio, as measured by the size of contributions. As at the end of the third quarter of 2016, net contributions for Family Takaful business grew by 8.7 percent on a year-on-year basis and accounted for 75.5 percent of market share of Islamic insurance business in the country. Malaysia is also recognized as the largest Family Takaful market in the world, with total contributions of around RM 4.8bn registered in 2014. On the other hand, the growth trend of the General Takaful business for the past five years has moderated to 11.4 per cent average annual growth for 2011-2015, as compared to the growth rate of 17.3 per cent in the years 2007-2010.[303]

This recent data show two important things; Islamic insurance is used more as an investment instead of protection, and individuals/families and not corporations or organizations are the main consumer of Islamic insurance in Malaysia. Family Takaful is like an endowment policy. A participant decides on the maturity period, the amount of annual contribution (provided it is above the minimum amount set by the company), and the frequency of contributions. The example of Family Takaful is an education fund. Insurance is seen by many Malaysians as an investment for which a return is expected.

On the other hand, General Takaful protects participants against losses from personal accidents and loss or destruction of property. The contract specifies the amount of contribution that the participant must make. Therefore, we will focus on analyzing Family Takaful to understand the 'social life' of Islamic insurance in Malaysia.

How is Islamic insurance presented to individuals or families in Malaysia? Before we discuss more detail on the preference of Malay on investment type of insurance instead of protection, we will elaborate how the concept of risk develops in the Islam modernist of the New Malay. Many studies show religion or belief system has correlation with the low level of insurance demand. Related to Muslim society of Malaysia, commutative contract of the mainstream conventional insurance is specifically objectionable by Sharia. This type of contract unduly limits uncertainty and ambiguity in human lives. Muslims can take steps to minimize the impact of

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[303] Hamim Syahrum Ahmad Mokhtar, Izwayu Abdul Aziz, and Noraziyah Md Hilal, "Corporate Demand for General Takāful in Malaysia," *ISRA International Journal of Islamic Finance* 9, no. 2 (2017): 164–184.

events, however, they believe that what happens is predetermined by God's will. For this reason, many Muslims see insurance as unnecessary. Furthermore, in their traditional environment in the villages, family and community is the one who will guarantee in a time of emergency.

The concept of risk is quite modern. The traditional society emphasizes on anticipation of the actual prevalence of life-threatening dangers which lead to economic insecurity. God or Nature is the source of this insecurity. Anthony Giddens argues that there has been huge historical transformation of the nature of risk -and security.[304] People in the modern age are relatively more secure than they were in previous ages. They have longer life expectation and freedom from serious disease. Nonetheless, the physical security of modern people is balanced by a new risk: war, nuclear threat, motor accident, environmental degradation, etc. These risks are not generated by natural causes, but as results of modern social organization or so-called abstract system[305] in Giddens' term. Furthermore, there is a 'globalization of risk in the sense of intensity' and extensity such as climate change and nuclear war. This new risk affects everyone or at least very large numbers of people on the planet. The intensification of worldwide social relations linking distant localities in such a way that local happenings are shaped by events occurring many thousands of miles away and vice versa.[306] Therefore, instead of anticipation, control of risk is an essential part of modern society.

As Malay migrated to the cities, worked in a corporate environment they have less access to their traditional community to provide that guarantee. They also face different types of insecurity: bankruptcy, expensive healthcare and college tuition, etc. welfare state situation, the state is the one who provide that as during the NEP, Malaysian state provide capital support, scholarship, and other material resources for the Malay society. State and market become crucial

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[304] Ulrich Beck also discuss the new nature of risk of modern society in his 1992 book on risk society. He argues that the modern society is facing different type of risk. It is a problem environmental hazard which cut across traditional inequalities of wealth and income. Furthermore, modernization dissolves traditional parameter of industrial society: class culture and consciousness, gender and family roles. Beck.

[305] Giddens defines abstract system as knowledge-based patterns of social behavior, coordinated through markets as well as bureaucracies, which govern the conditions of individual existence. The spread of these systems is global: 'In high modernity, the influence of distant happenings on proximate events, and on the intimacies of the self, becomes more and more commonplace. Giddens, *The Consequence of Modernity*.

[306] Ibid.

actors because the traditional institutions and culture can no longer provide the necessary protection for modern people.

Patricia Sloane mentions one interesting example of how the understanding of risk developed among the New Malay. The establishment of Amanah (investment trust for Malays) by two Malays entrepreneurs is relevant to this case. It can help us to understand how people perceive Islamic insurance. The founders understand that the abundant NEP-era educational resources for Malays would not be around forever. Moreover, the government seemed to require that Malays begin to take an ever-greater group and individual responsibility for their own development-what they felt was the message behind Vision 2020-they believed that Malay parents would soon need to put away money to pay for university for their children. Through Amanah, Malay parents would learn to take responsibility for educational development of their own children; investing small amounts money in the trust every month for 18 years, parents would be able to draw out a substantial sum when their children were ready for university.[307]

The awareness of risk and future uncertainty mark the New Malay identity as a modern and entrepreneurial society. Investment is a language of modern society, particularly the one who embrace entrepreneurship as their identity and social status. On the one hand, it is the New Malay's way to distant themselves from the lazy and fatalistic traditional Malays. On the other hand, Islamic insurance is understood not as a way to control uncertainty, but as an idiom of care responsibility for their family. Furthermore, subscribing to an Islamic insurance policy to protect themselves and invest on the family future are seen as performing religious duty by the New Malay generation. Naail Mohammed Kamila and Norsham Binti Mat Norb present an interesting interview result on how preparing for future risk is understood as part of being a good Muslim:

> Takaful and religion are very much close to each other. Why? Because in religion, in Islam (we're talking about Islam). So, I refer to Islam, not other religion. In Islam, we have this Maqasid of Sharia (the objectives of religious law). So, one of the objectives in this Maqasid is to protect your wealth. In that sense, we're buying Takaful not only for us but also for our generations. An example is when you're buying a Family Takaful product. Maybe you're protecting yourself for now so that not burden your family. In case of any emergency, you must be hospitalized, you're

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[307] Patricia Sloane, *Islam, Modernity and Entrepreneurship among the Malays* (Palgrave Macmillan UK, 1999).

well protected. Then, and anything happen to you, also, maybe your family you left behind will get some compensation. [308]

Investment is not perceiving merely as a worldly affair but as a religious duty. Being mindful of the uncertainty of the future and prepare for that is a way to achieve the objective of Sharia. Islamic insurance in Malaysia serves as both protection and investment functions. Islamic insurance in Malaysia has been presented as a modern way to deal with future uncertainty, particularly in the condition with less government assistance. Buying an insurance policy is also considered as a noble act that shows a self-reliant attitude. The attitude that inherent in their entrepreneurial identity. Moreover, Islamic insurance is not presented as a tool for controlling the future. This would be considered by the Malays as an act of underestimating the power of God. The Malays reject this type of secularism. Rather, Islamic insurance is presented as an idiom of care responsibility toward the family.

Investment is considered by the Malay entrepreneur class is an act of piety. For the first generation of the New Malay during the first decade of the NEP, investment and being frugal are entrepreneurial ethics that consistent with Islamic values. This view is a rationalist view that has been promoted by Islam modernists. However, for the Sharia generation who came after them, the act of investment and business activities, in general, has to be conducted consistent with Islamic values. It has to be Sharia-compliant.

Sloane argues that Sharia has also emerged as a novel form of corporate culture, reconfiguring workplace identities and relations in distinctly Islamic ways many see the growing appeal of the Islamic economy in Malaysia not just as an ethical place to bank and borrow, but as a place to work. Sloane quotes one young woman who captured this desire well: "We want to know that the money with which we feed our children was earned morally."[309]

The perspectives on Islamic business activity of the early Malay entrepreneurs are parallel activity to that of Calvinist businesspersons described by Weber, in which work provides rewards to capitalists in both this world and the next.[310] However, the latest Muslim businesspersons in

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[308] Kamil and Nor.
[309] Sloane-White.
[310] Daromir Rudnyckyj, "SPIRITUAL ECONOMIES: Islam and Neoliberalism in Contemporary Indonesia," *Cultural Anthropology* 24, no. 1 (2009): 104–141. Page. 129

Malaysia Islamic economy perceive it differently. For them, Islam has its own terms for understanding rewards and salvation that do not rely on a Eurocentric model.

From her field study, Sloane found out that it was evident that an increasing amount of Arabic- and Qur'an-influenced teaching and knowledge was reflected in their experience, compared to the preceding cohort of Malay entrepreneurs she studied a decade earlier, whose Arabic and Qur'anic backgrounds were less developed. The men she interviewed, now mostly in their forties, were raised and educated in an Islamized Malaysia. Now many of them participated in rigorous study groups that combed Islamic texts for connections between religion and economic life and worked closely with local religious teachers and *Ustaz* to understand the rules for commercial and organizational life contained within the Qur'an and the Hadith.[311]

Naail Mohammed Kamila and Norsham Binti Mat Norb also notice the importance of Sharia-compliant in the decision to buy Islamic insurance. Two of their respondents emphasize the important of Sharia compliance in the daily life of Muslims. Therefore, providing Islamic scheme for financial protection is an urgent need nowadays. According to them, the compliance toward Sharia in economic activity is the indicator of a good Muslim. Moreover, Islamic insurance is not considered simply as a financial product, but it is part of way of life.[312]

Islamic insurance has been promoted as a scheme that carefully designed by following the injunction of Sharia in the business transaction. The companies claim that the scheme has been approved and continuously monitored by Islamic scholars who are expert on the field. Moreover, they emphasize on where the money is invested. The money must be invested in lawful businesses according to Islamic teachings. This is an important aspect of Islamic insurance in a low insurance demand society.

Indeed, many Malaysian Muslims today are firmly placed within the urban middle classes. Many live and work in and around the capital city of Kuala Lumpur, employed by private-sector corporations. They have higher income that for many researchers as an important factor for insurance demand. However, as we see in Malaysia, the demand for Islamic insurance is not merely drive by the changes in the socio-demographic factors. There are ideologies and norms

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[311] Patricia Sloane-White, "Working in the Islamic Economy: Sharia-Ization and the Malaysian Workplace," *Sojourn: Journal of Social Issues in Southeast Asia* 26, no. 2 (2011): 304–334.
[312] Kamil and Nor.

with far-reaching social impact, as more and more Malaysian Muslims seek to calibrate their politicoreligious orientations to their economic practices, a process Johan Fischer has called "halalisation".[313]

Insurance plans may be problematic in places where it has long been customary to gift or indirectly pay the government and indigenous practitioners for services as an incentive for good care or to forge personal relationships.[314] Islamic insurance facilitates the transition of the Malay society to become more self-reliant and less dependent on the state and society but maintain Malay's traditional value helping each other. In Kamil and Nor, two of their respondents explain this idea further. In the word of one of the respondents:

> The most important thing in Takaful is helping each other, is a mutual corporation or benefit. Yes. Ta'awun. In that sense, is what our religion, in Islam that we have to help each other. So, when we invested in Respondent (S1) said Takaful product, we already made ahead that this payment will go to who participated in that. The pool of fund can be used to help those people in difficulties. At the same time also, if we are in that situation, the unfortunate one, so the same thing will happen. The same pool of fund will be used to protect us, to compensate us. And then to the Tabarru' fund, if there any excess to it, it can be shared among the participants. It's something that other conventional not doing it…[315]

The Malay entrepreneurship is unique. Instead of forging individualism for entrepreneurial success, it emphasizes obligation to others. The others might be understood narrowly as fellow Malays, or even the nation. They believe that Muslims in Malaysia should all participate and support Islamic insurance because by doing so, they are strengthening Muslim position in the country, improving their funds to assist our Muslim brothers and sister as well. [316]

Furthermore, behind its increasingly sophisticated financial plan, Islamic insurance represented what they described as a 'truly Malay organization', both spiritually and communally focused. It was marketed to a network of Malays-who were moved by the idea of caring for others. In their understanding, Islamic insurance brings double rewards: this-worldy and other-

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[313] Fischer, Johan. "Manufacturing Halal in Malaysia." Contemporary Islam 10, no. 1 (2016): 35-52.
[314] Datta 2014; Nichter 1983.
[315] Kamil and Nor.
[316] Ibid.

worldly-rewards. It could anticipate current and future risk, therefore, protection for the members, and also the religious reward of helping each other. It is social tools that provided multiple rewards, instruments of convergence of devotion to others and to Allah, the means to an exemplary virtuoso identity. Islamic insurance is perceived as representing mutual, network *gotong-royong*, compares to the conventional insurance, which is considered exploitative, untrustworthy, greedy therefore un-Islamic.

The Takaful Act 1984 mentions that company and cooperative can offer Islamic insurance product. Historically, insurance was initially provided by self-organized mutual societies (guild) in the nineteenth century and then pushed aside by the rise of corporate insurance companies and statutory social insurance in the twentieth century. Many Islamic scholars argue that mutual or cooperative structure is more appropriate for Islamic insurance. Nonetheless, most of the Islamic insurance products in Malaysia are offered by for-profit companies. How this for-profit motive does not impede the growth of Islamic insurance in Malaysia?

The general acceptance for for-profit entities cannot be separated with the positive attitude of Malay society toward entrepreneurship. Islamic insurance develops in the entrepreneurial environment of Malaysia. Sloane summarizes Malay entrepreneurial ideology as a whole: "The claim that in development, duty to others must be stated and shown; the belief that one must not seek greedily the fruits of success but must generously invite others to partake; the insistence that entailments-be they profits, contacts, or opportunities-must be rightfully earned through effort, sincerity, and hard work; and, perhaps most crucial of all, the perception that the entrepreneur is the cornerstone of modernity, possessing the ability to transform simultaneously both society and the economy into the image of development espoused by the Malay Muslim doctrine of virtue and the Mahathir government."[317]

Compares to Indonesian society, the Malays has a very high trust in private sector. They do not have an issue with profit-motive seeking as long as it is pursued with the guidance from the religion. Moreover, they do not have a reservation of having foreign-owned Takaful companies.[318]

[317] Sloane, page 174.
[318] Kamil and Nor.

A certain degree of institutional trust is necessary for people to pay into an insurance program, raising the need for sustained attention to this concept. How is institutional trust established above and beyond trust in the advocates of particular insurance programs? In Malaysia, the government has a prominent role in developing this trust. The government spend a lot of money to build the regulatory framework, institutions and educate the public to support Islamic finance. Although the Malaysian government acts mostly as an incubator and not a direct participant, public sees the image that Bank Negara Malaysia controlling over the business as mentioned in the interview above.

Furthermore, government involvement, in this case, has not seen as a negative thing. Moreover, Islamic insurance develops in environment where there is a tight connection between Islamic money and Islamic authority. Sloane mentions that these Malay entrepreneurs often criticized NEP for providing "handouts" to Bumiputera, because Sharia does not allow earnings from transactions that do not involve work. But they did not question the staggering amounts of money being channeled by the government and its institutions and by corporations to serve and promote Islam and the cause of God. Nearly 1 billion ringgits is allocated yearly from Muslim and non-Muslim taxpayers to JAKIM, and huge sums are funneled into institutions and foundations that, according to Malaysian tax law, are meant to advantage all Malaysians of all ethnicities and religions. But that tax money often actually funds explicitly Islamic activities and singularly Islamist ones, while at the same time government policies restrict the kinds of tax advantages available to non-Muslims. Criticism of government institutions and policies that provide resources and benefits to Muslims and deny them to non-Muslims is always rare in Malaysia because of laws that restrict freedom of speech.[319]

The emergence of the 'New Malay' entrepreneurial class

The face of Malaysia's capital city, Kuala Lumpur, today is entirely different from the year 1969. The year when ethnic riots happened in Malaysia. The 13 May 1969 (mainly) Malay–Chinese sectarian violence — one of the darkest episodes in Malaysian history in which hundreds of people lost their lives. The proximate reason appeared to be the result of ethnopolitical

[319] Sloane-White.

conflicts in the aftermath of the 1969 general election. The deeper cause, however, was said to be Malay dissatisfaction with their role in the modern economy, and their perception that the Chinese had monopolized all economic activities in a nation which, the Malaysian Constitution stated, rightfully belonged to the indigenous Malays.[320] There was a fundamental contradiction within Malaysian society-the concentration of wealth in the hand of the wealthy Chinese and monopoly of political power in the hand of Malays. Nowadays, it is common to see a Malay name after the title of CEO, manager or director of national or multinational companies. These group of people represents the new entrepreneurial generation of Malays or so-called New Malay.

The New Economic Policy (NEP) was inaugurated in 1971 as a response toward that ethnic conflict. NEP was affirmative policies and strategies provided by the state with the means to help the Malays or Bumiputera. This policy replaced the essential laissez-faire economic framework established in Malaysia upon Independence. Within the 20-year timeframe (ran out 1990) it was expected that the economic equity vis-à-vis the Chinese would be reached when it could be demonstrated that Malays had reached 30 percent ownership of and participation in all industrial and commercial activities. To reach this goal, an enormous transformation and expansion of economy was set in motion, leaving almost no institutional apparatus untouched. There was a huge increase in the number of ‘quasi-public bodies and government agencies that were charged with aiding program for Malays or that acted as surrogate institutions for the transfer of capital shares and ownership to Malays. Over 20 years, Kuala Lumpur was transformed into a modern city, built to support the growing policy-led enterprise sector and the public and private interests of the mushrooming Malays middle class which have been educated to serve them.[321]

NEP program was designed to increase the percentage of Malays working in the non-agricultural sector, particularly in the managerial level, and increase the wealth of the Malays. [322] The program gained success in reducing poverty among Malays and in creating Bumiputera middle class. However, some critics suggest that the idea of creating a new and self-sufficient Bumiputera through affirmative actions, while compelling and impressive (to a certain degree) at the macro level, did not appear to have materialized at the micro level. This New Malay group

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[320] Sloane.
[321] Ibid.
[322] R. S. Milne, "The Politics of Malaysia's New Economic Policy," *Pacific Affairs* 49, no. 2 (1976).

according to this view is a mere reflection of privileged political access within the patron-client relationship of Malaysia's political economy system. Adding to that, the long-term implementation of racially-targeted policies reinforces stereotypical ethnic identities and hinders the creation of a more inclusive society."[323]

Within three years of the NEP implementation, 98 percent of all those recruited for government service were Malays, a percentage that far exceeded the 4:1 Malay ratio. During the period of the Second Malaysia Plan, Malay employment in the commercial and industrial sectors rose rapidly to parallel the rate in the public service. [324]Similarly, Malay admissions to institutions of higher education also increased dramatically. Malay student numbers at the University of Malaya, for instance, increased from 49.7 percent to 66.4 percent between 1970 and 1979. The government also actively participated in funding Malay students for overseas studies.[325]

The NEP also provided an avenue for Malays to mobilize their capital and increase their savings. This was achieved through the establishment of agencies such as the Pilgrims Fund Board or *Lembaga Tabung Haji* and National Equity Corporation or *Permodalan Nasional Berhad* (PNB). During the Islamization project, the government spends more funding for the establishment of several institutes to support the development of Islamic finance.

Although the NEP managed only 19.4 percent of Malay ownership of public companies in 1990 against the target of 30 percent, it did create an enlarging Malay middle-class and more professionals so that by 2004 there were, in fact, more Malay doctors than Chinese doctors.[326] The presence of these Malays in various professional and employment sectors had, in some ways, helped to restore Malay confidence and the perception that the NEP had helped the Malays to improve their standard of living and economic position.[327] A significant outcome under the NEP was the creation of government-owned entities that became directly involved in the commercial activities of the nation.[328]

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[323] Gomez, Saravanamuttu, and Mohamad.
[324] Means 1991.
[325] Milne.
[326] Kessler 1992: 145; Sowell 2004: 70.
[327] Patricia Sloane, "Reason and Passion. Representations of Gender in a Malay Society (Book Review)," *Oceania* 69, no. 4 (1999): 304–305.
[328] Jesudason 1989: 72, 86-100; Searle 1999: 58-78).

In overall, the new Malays class share similar experiences. Most of them were socialized for elite roles by civil-service parents. They went to English-style educational system and then continued to overseas or local universities. More importantly, they were rewarded with sponsored opportunities for increased legitimacy and power in the modern economic system.[329] They also tend to live the same neighborhood of the cities. In the 1970s, there was rapid Malay urbanization of Kuala Lumpur and its surroundings. Quotas were established to ensure that new communities reflected blended racial make-up. However, people continue to live in traditionally racially segregated areas in most of the city.

Many critics on the NEP argue that the affirmative program gained success in poverty reduction but failed in creating Malay entrepreneurship. Gomez describes Malay entrepreneurship as mere reflection of a patron-client relationship built among Malay businesspersons and Malay politician, rent-seeking activities, and political privileges, and powerful Malaysian state. Nonetheless, many field studies suggest that there has been a radical change in the mindset of this small New Malay class that gave profound influence in general Malay population. Entrepreneurship has been embraced by many not only as an actual occupation but as their new identity, aspiration and social status.

They believed that full equality with the Chinese would be reached when Malays had become true capitalist owners and producers themselves. Many of them, in addition to holding down professional jobs in two-career families, had ambitious plans to prove that Malays were as business-minded as the Chinese, and were engaged in multiple entrepreneurial plans and projects. Indeed, even many of the Malay men and women in civil-service and other wage-paying positions, the 'bureaucratic middle class', the classic Weberian no-risk category of 'the middle class' in historians' analyses of western classes, had some form of an entrepreneurial plan in the process.[330]

Furthermore, they understand that entrepreneurship is not only a way to achieve wealth but it also a way to serve God and others. It is often quoted that Prophet Muhammad was a merchant himself. Business venture requires hard work, intelligent, and perseverance which

[329] Sloane, *Islam, Modernity and Entrepreneurship,* page 45.
[330] Ibid.

according to them the qualities that every Muslims should have. Furthermore, having your own business means you are independent and do not rely on other people or government to assist you. Business creates jobs. Being an entrepreneur means being a good Muslim and helping people and the nation.

This class possesses modernizing ideas, which is different from the old attitudes of Malay Muslims in Kampong or villages. The new Malay claimed to be a hard worker, modern and entrepreneurial compares to the lazy, traditional and dependent Malay in the kampong or the village. This identification actually was part of contestation between Barisan National and PAS, particularly during the Islamization process of the 1980s. Islam was a moral standard in this political contest. Mahathir offered his vision of so-called modernist Islam: 'using the rhetoric of rational interpretation of Islam's teachings, and with his political preoccupations in mind, he adapted classical modernization theory so that it can accommodate Islamic principles and has elevated those Islamic teachings which can be argued to encourage entrepreneurialism.' Islam for the modernist Islam is a guide to motivate Malay Muslims to thrive for the modern lifestyle, economic dynamism, and tolerance. [331] Meanwhile, PAS was discredited as a group of zealots who cannot face up modernity.

This New Malay identity is not purely constructed out of Muslim identity. There are Muslims in Malaysia who are not Malays-such as Indian, Arab, Filipino, Thai, Bangladeshi, and Indonesian Muslims- are often not perceived to be 'genuine Muslims', and therefore are generally held outside the boundaries of Malay amity and affect. Nevertheless, these demonstration of social marginality within the Muslim community are relatively insignificant by contras in relation to Chinese. Chinese area considered as social and economic outsiders representing a threat.[332]

Although, Malays admire the hardworking and frugal characteristics of Chinese businesspeople, they are considered as a lack of social virtue. Chinese is claimed to be greedy, cheater and self-centered, while Malay is claimed to be more open, hospitable, and generous. They also rejected what they understand as the characteristics of Western entrepreneurs: the

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[331] Malhi in *Malaysia: Islam, Society and Politics*.
[332] Sloane.

unethical and egoistic business ventures. Malays see themselves as virtuoso entrepreneurs: submissive, other-centered, and altruistic.[333] Islamization certainly strengthened the idea that Malays are modern, but they are different from the Western or Chinese entrepreneurs. This mentality is what Joel S. Kahn as “self-exoticising discourse” meaning while acknowledging their status as modern and entrepreneurial, many Malaysian also claim that their entrepreneurship culture is unique.

Decades of Islamization since the 80s gave birth to what so-called Sharia generation.[334] While they have similar socio-demographic indicators like their parents of the first NEP generations, they have more awareness of Sharia-related issues. They continued the modernist Islam ideas and practices of the previous generation, but they have stricter observance on Sharia. They gave more in charity because the Sharia obligation of zakat, save their money in the Islamic banking, they concern on ensuring their business transactions are Sharia-compliant, and many of them work in Islamic financial institution. For them, Islam is not only regarded as ethical values in business but also a ruling and technical instruction in business.

Many of them see the NEP had emphasized on ‘Western-style’ of profit accumulation with usury and individualism. Now they felt they knew much more about Islam and its Sharia requirements and could fully embed religious principles and moral practices in their economic ventures and all realms of their modern lives. They are the corporate Sharia elite. Among them were Sharia advisors with Islamic pedigrees who set the standards of Islamic finance, authorizing the Sharia compliance of financial products in the Islamic economy, marketing their expertise and scholarship globally, and serving as business consultants to equally successful corporate executives and owners. Connected to each other through business interests and membership in Islamic study groups and Islamist pressure groups, the men of the corporate sharia elite shared a vision of a new kind of virtuous capitalism – one that would not only refashion the economy and people of Malaysia in Sharia-compliant ways but also serve as a model for Muslims worldwide, and perhaps even remake capitalism for the world.[335]

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[333] Ibid.
[334] Patricia Sloane-White, *Corporate Islam [e-Book] Sharia and the Modern Workplace*, 2017.
[335]Ibid.

The relationships between the New Malay and 'traditional Malay', between Malay with other the 'not-genuine' Muslims, and between Malay with Chinese show the exclusionary power of Malay entrepreneurship. However, it also as an inclusionary power among the group member itself. Their relationship with other elite Malay business leaders and politician is not seen as a traditional feudal or patron-client relationship. They see their relationship as self-and-group empowering network based on self- reliant, egalitarian, and meritocratic capitalist society.

Furthermore, Malays see themselves as affectively bound, dutiful, real and symbolic kin, mutually entailed by obligations, and threatened by others. The centrality of entrepreneurship in this New Malay lives corresponds to the increase in the importance of material wealth in their social relations. Malay life in relationships with parents, spouses, cohorts and the communal group is bounded by Islamic duty and financial obligation. For example, the Dakwah activities have influenced Malays to be more charitable by performing zakat. They are feeling more responsible financially for supporting their relatives.

The goal of creating Malay entrepreneurs through the NEP might not be achieved as expected, but certainly, there has been radical transformation on how Malay perceives entrepreneurship, particularly during the implementation of Islamic finance project. Entrepreneurship has become the main vector of ethnic, religious, and moral worth and a test of virtue and modernity among the beneficiaries of NEP or so-called New Malay. The affirmative policy of NEP created rapid social transformation where Malay received an abundance of wealth and opportunity. This condition created an 'altered' identity of Malayness. They rejected the stigma of lazy and backward Malays. They claim themselves as modern, entrepreneurial, and pious Muslims. Entrepreneurship demonstrates the process by which moral obligation to others, hard works, and Islamic faith have become symbolized together in economic activities, which are at once 'modern' and 'Malay' and later on, also 'Sharia-compliant'.[336] The interpretation of Malay entrepreneurship by stressing on the obligation to others, Islamic values, and self-reliant are significant on the development of awareness among the New Malay on the concept of risk, therefore susceptible for the development of Islamic insurance.

[336] Sloane, page 16.

Conclusion: harmonization and Muslim capitalist modernity in Malaysia

The success of the institutionalization of Malaysia's Islamic insurance industry is primarily attributed to the gradual and systemic approach driven and backed by the state. Unlike many Middle Eastern countries, there is no single entrepreneur pioneered the overall Islamic financial institution in Malaysia.[337] Prime Minister Mahathir Mohamad himself was the one who ordered the formation of a task force to explore the viability of an Islamic insurance company in Malaysia in October 1982.[338] However, the state has taken a managerial role that can incubate a new service economy in which private individuals and institutions (not the state) are the primary agents of economic growth. The Malaysian state created the necessary infrastructure to facilitate the emergence of viable national and transnational Islamic financial systems but did not become involved in creating commercial firms.[339]

Furthermore, Malaysia's Islamic insurance and Islamic financial institutions, in general, have served as a locus where the secular Malaysian government, represented by Barisan Nasional *(BN)* under the leadership of Mahathir Mohammad, to create a coalition with the modernist and urban Malay Muslims, to strengthen the economy of the Malay ethnic group or *Bumiputera*. Even after the resignation of Mahathir Mohammad in 2002, Abdullah Ahmad Badawi, prime minister from 2003 to 2009, persisted with a developmentalist model that promoted *Bumiputera* capital, but he showed little interest in developing Malay – or Malaysian – big businesses. He advocated more on policies that nurtured SMEs, including industries dealing with halal products, dominated by poor rural Malays, as well as supporting many new Islamic insurance companies.[340] This political strategy has enabled BN to preserve and consolidate its continuous dominance against

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[337] Emmy Abdul Alim, *Global Leaders in Islamic Finance: Industry Milestones and Reflections* (Singapore: John Wiley and Sons Singapore Pte.Ltd., 2014).
[338] Rajesh Babu, "Tun Dr Mahathir Receives Tokoh Takaful Award," (6 November 2009), accessed 25 September 2018, . http://www.ssig.gov.my/blog/2009/11/06/malaysiadr-m-receives-award-for-outstanding-contribution-to-takaful-industry/.
[339] Rudnyckyj.
[340] 87 percent of SMEs are in the services sector, 7.2 percent in manufacturing and 6.2 percent in agriculture. 99 percent of firms in agriculture are SMEs. Key sub-sectors within services comprise those related to Islamic financial products, including banking and *Takaful* (Islamic insurance). See Malaysia (2006: 166-67) for further details about public programs to aid SME development.

the threat from the traditional and fundamentalist Muslim groups represented by Islamist political party of PAS, and also from the Chinese minority.

The Islamic financial institutions were designed and regulated to enhance Malay population's participation in the development process. It is created as an alternative avenue rather than a replacement for the existing economic system. It contributed to the savings mobilization and capital accumulation of the Malays in order to improve their standard of living and bring them up to par with their fellow citizens of Chinese origin. The creation of these institutions enabled the Malaysia state to make important concessions to the Muslim interests and Muslim identity of the Malay majority, to defuse the political pressures from the Islamist political party, and to accommodate its Chinese and Indian minorities and the capitalist structure of the economy. All of these has been part of a bigger goal for harmonizing Islamization with economic liberalization.

The Islamization drive has provided Mahathir with a way to position himself as a defender of Islam and Malay identity, and to embrace the calls for more Islam in public life, to counter critiques of the ruling government of Barisan Nasional (BN) as 'secular' and therefore spiritually bankrupt. Arguing for 'secularization', as classical modernization theorists would have it, would therefore unhelpful to Mahathir. Thus, he has argued instead of Malaysia to modernize Islamically, using his favored, pro-capitalist Islamic teachings and creating an Islamic rationale for the familiar prescription for modernization. Islam, for him, is a moral guide, not politics of Islamic state, but a set of values and ethics to guide an individual or privately managed action, to motivate Malay Muslims to act in a way which is conducive to national unity and economic growth. In pursuing modernization and economic growth, the BN has focused on creating and cultivating a small Malay entrepreneurial class, which possess modernizing ideas and can lead Malay Muslims away from their 'traditional' attitudes. The BN has had to discredit the Islamist political party of PAS while ensuring that its own followers also appear sufficiently Islamic. BN's attempt in this area have involved mobilizing selected Islamic teachings, such as those which make allowances for the accumulation of wealth and presenting them as the fundamental of

Islam. Mahathir has tried to present his government as an Islamic one. Competition between BN and PAS was the main driver for Mahathir's Islamization of society and state.[341]

Islamic finance project has been considered as the most acceptable of Islamization of Malaysia. Rather than creating tension as happened in the Islamization of Malaysia's legal system, Islamic finance is allowing a Muslim elite to operate adroitly within (and profit from) capitalism, and welcoming Muslim and non-Muslim investors alike. This reality includes the development of Islamic insurance or Takaful. Malaysia Islamizes its insurance through the institution of Islamic insurance, which is developed as an alternative and not a substitute for the still available conventional insurance. Malaysia model of Islamic insurance is Sharia-compliant but regulated under secular legislation. The development of Malaysia's dual finance system is tied up with its social and economic policy and that is why it was fully supported by the country's top leadership in addition to the Central Bank, the Parliament, and the public in general.

The Government of Malaysia is also using Islamic finance in general for its key entry to globalization. Malaysia was of the first countries to take a systematic planning approach to develop the Islamic finance system for continuing future progress of its financial industry's rapid development. Malaysian government through Bank Negara Malaysia (BNM) invites financial institutions across the world to establish Islamic insurance and Islamic re-insurance operations in Malaysia to conduct foreign currency business. Altogether, Islamic insurance was a result of the convergence of diverse interests among political coalitions within Malaysia polity.[342]

The second reason for the impressive development of Islamic insurance in Malaysia relates to the social process within Malay society itself. The religion of Islam played a pivotal role in the state's development strategies by fostering New Malays with characteristics supportive toward economic development (such as diligence, accountability, and education). Furthermore, by promoting a form of Islam fully compatible with its development objectives, the state made it

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[341] Amrita Malhi, "The PAS-BN Conflict in the 1990s," in *Malaysia: Islam, Society and Politics : Essays in Honour of Clive S. Kessler/ Edited by Virginia Hooker and Norani Othman* (Singapore: Institute of Southeast Asian Studies, 2003), 236–65.

[342] Patricia Sloane-White, "Islamic Finance and Muslim Capitalist Modernity in Malaysia," *The Caravan*, 1715 (27 September 2017), accessed 18 April 2018, https://www.hoover.org/research/islamic-finance-and-muslim-capitalist-modernity-malaysia

possible for “government policies [to] seek to bring Islam in line with capitalism”.[343] This mindset originated long before post-colonial Malaysia.

It was an outcome of a social formation inherited from the British rule in Malaya prior to independent Malaysia. The British Empire consolidated the apparatus of centralized government and its capitalist economy, but at the same time, ‘weakened’ or coopted its civil society. The combination of a centralized government, the coopted religious institutions, and a capitalist economy leads to a higher trust toward Islamic insurance industry in Malaysia. The ‘weak civil society contributes to the inability of Malaysian society in establishing institutional frameworks of economic security outside the market mechanism. Historically, Malaysia has a weak informal network such as *Waqf* (religious endowment). The waqf institution has long been neglected and nearly forgotten by the Islamic community in Malaysia as compared to the other Islamic institutions). [344]

However, at the same time Malays can use their social network for economic ends. Malays has demonstrated their *kampong* values-sharing, fairness, equality, and balance- into a modern and entrepreneurial society of Malays. For Malays, among the Malay middle class, entrepreneurship has become the main vector of ethnic, religious, and moral worth, and a test of virtue and modernity among themselves.[345] Rudnyckyj terms this assemblage 'market Islam' and contrast it with what has been labeled 'civil Islam'. He argues that, “market Islam seeks less to create commensurability between Islam and democracy and is instead designed to merge Muslim religious practice and capitalist ethics. Market Islam is thus less concerned with state power and the articulation of politics and religion, and more focused on eliciting the ethical dispositions conducive to economic liberalism.”[346] The truth of that statement can be seen from the Malaysia’s Islamic insurance development that is increasingly stressing on its market viability and Sharia-compliant contract rather than the mutual organizational framework of Takaful.

Neslihan Cevik’s work on “Muslimism” in Turkey seems to be relevant to explain the development of Islamic insurance as part of Islamic revivalism within Malaysian society. In her

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[343] Ong.
[344] Hisham Yaacob, *Waqf History and Legislation in Malaysia: A Contemporary Perspective*, vol. 3 (2013).
[345] Sloane.
[346] Rudnyckyj.

study, she shows how Islamic revivalism in Turkey has manifested itself in Muslims' engagement in the markets, political parties, and civic society while still adhering to the Islamic ideals. The new Islamic form of Turkey encompasses all aspects from economic and political, to cultural expression along with its theological structure.[347]

This innovative concept was built on a vibrant empirical research of the post-1980 Turkey. Cevik uses the terms 'a guilt-free modernity' and 'Islam without apology' to describe this attitude, which cannot be reduced either to political adaptation or commodification of Islam. "It emerged in everyday life spaces in a quest to establish new institutions and lifestyles that allow Muslims to rework aspects of modernity".[348]

This hybridity is located analytically and based on the notion of "Islamic three ds", corresponding to major dimensions of the Islamic heritage: din (religion), dunya (this world), and dawla (the state). She analyzes the 3ds based on the ontology, agency, and action. The purpose is to differentiate Muslimists from Islamists. For instance, in the level of ontology in the dimension of *din* or religion, Islamists perceive Islam as an ideology, while Muslimists understand it as identity. At the level of the agency of *dunya* dimension or worldly affairs, Islamists tend towards communitarianism, while Muslimists are more focused on individuation. At the level of action of *dawla* dimension or the public sphere, both approaches are different in terms of how to create social improvement. Islamists have a state-cantered political action, while Muslimists use a broad social action. Islamists (just like secularists) claim to be the guardians of 'traditions', while these Muslimists seek to find innovative ways of dealing with the world.[349]

[347] Neslihan Cevik, *Muslimism in Turkey and Beyond: Religion in the Modern World* (New York: Palgrave Macmillan, 2016).
[348] Ibid.
[349] Ibid.

CHAPTER IV

INDONESIA

Despite sharing so many similarities, Indonesia and Malaysia are achieving a different level of Islamic insurance development. Malaysia has become the hub of Islamic finance of Southeast Asia and the world, while Indonesia still has a vast untapped market. Although both countries started the Islamization and privatization processes of their economy in the 1980s, the Indonesian Government gave official support for the establishment of Islamic financial institutions in Indonesia only after 1990s. Islamic finance, in general, was officially introduced in 1992 and Islamic insurance in 1994 with less government commitment and bottom-up approach. However, Indonesia Islamic insurance sector recently has been showing a significant growth by having a contribution of 19% of the total regional market. In 2016, Islamic insurance accounted for 6.2 percent of the overall Indonesia insurance market with asset more than 42 trillion IDR (3.1 million USD).[350]

Islamic insurance was introduced officially to Indonesian society through the establishment of PT Syarikat Takaful Indonesia (Takaful Indonesia) on 24 February 1994. It was the first Sharia-compliant insurance company in Indonesia. It was endorsed by ICMI (Indonesian Association of Muslim Intellectuals) and promoted through Islamic informal and formal organizations. Up until now, Islamic insurance in Indonesia has developed into 20 Family Takaful companies, which consist of 3 Family Takaful companies and 17 units of Family Takaful, and 25 General Takaful composed of 2 fully-fledged Islamic insurance companies and 23 units, and three Islamic re-insurance windows.[351] The introduction of the new insurance law of 2014 was partly responsible for this positive development.

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[350] Financial Service Authority of Indonesia (OJK), *Daftar Perusahaan Asuransi Umum Syariah 2015* (translation: List of Shari'ah insurance companies).
http://www.ojk.go.id/Files/statistik/26102015daftarperusahaanasuransisyariah.pdf

[351] Srikandi Utami, "What does the future hold for the Takaful industry in Indonesia," *Srikandi Utami, "What Does the Future Hold for the Takaful Industry in Indonesia " (2014).*, November 2014.
http://islamicfinancenews.com/contents/roundtables/indonesia/Indonesia.pdf . Islamic window refers to commercial bank or insurance company that offers Islamic insurance products.

Furthermore, there has been a growth in the form of Islamic micro-insurance for the poor population and waqf-insurance products in Indonesia. Islamic micro-insurance has been utilized to help the poor, especially in rural Indonesia. Indonesian poor only need to buy monthly premium of 5,000 Indonesian Rupiah (50 cents) to receive proper health care against dengue fever. The waqf-insurance links insurance protection with a social endowment. With monthly payment, Muslims in Indonesia can contribute to the social cause by investing in property such as mosque, school, and hospital, and t the same time, receive financial protection for sickness and death. The development of Islamic micro-insurance and waqf-insurance in Indonesia represent the bottom-up approach of its communitarian tradition that has provided a strong foundation for the national economy.

This chapter examines the reason behind the existing gap and differences between Indonesia and Malaysia (also Pakistan) in Islamic insurance. It starts with a brief introduction of Indonesia as a multi-cultural religious state, which stresses on the status and role of Islam in the state building, its plural and dynamic society, and the dualist economic system of Indonesia. Unlike in Malaysia, Islam does not have special status compares to other five official religions in Indonesia. All of six official religious groups receive state funding, representation in government, publicly funded religious institutions and legal protection.

The next section provides detail information on the growth and institutional development of Islamic insurance in Indonesia. This section also discusses the linkage between Islamic insurance with other social tools into the broader context of insurance or social protection in Indonesia. Historically, the state has been heavily involved in providing that protection to Indonesian citizens, and the private sector has never been the primary provider for economic security in Indonesia. Recently, Islamic NGOs have become the most important actors in this matter.

The following two sections explain the factors for Indonesia's Islamic insurance development through the lenses of 'political life' and 'social life' of Islamic insurance. The political life of Islamic insurance section explores the catalysts, the political landscape of Islamic insurance in Indonesia, and the political coalitions behind Islamic insurance, particularly during the repressive government of President Soeharto regime (1966-1998) since the 1980s. Islamic

insurance and other Islamic finance institutions were initiated in the periphery led by non-state actors. Many scholars argue that this dynamic has been generating both authentic and Islamic version of financial institutions, such as Islamic micro-finance and waqf-insurance schemes. The second part elaborates Indonesia's social transformation, which is responsible for the development of the expression of Islam in their ideals for the nation-state of Indonesia and economic ethics. Indonesian's communal economic ethics is influential in the development of Islamic insurance in Indonesia. For many Indonesians, maintaining harmony and social solidarity are more valuable than personal freedom and achievement. Understanding socio-economic ethics is vital to make sense of the development of Islamic insurance in Indonesia.

The structure of a religious state

This section provides a brief introduction of Indonesia as a religious 'imagined community', particularly in its relation to the role of Islam in building a religious state, its multi-ethnic/religious circumstances, and its economic structure. Both legal and societal facts show the significance of religions in Indonesians' lives. The Constitution declares Indonesia as a religious state, protects religious freedom, and supports religious communities. For many Indonesians, religion is essential, not only in the formal sense of implementation of religiously inspired laws, but religion is considered essential in creating an ideal society.[352]

However, Indonesia is also a country rich with paradoxes. The paradoxes are the result of its long historical and social-cultural processes, particularly colonialism. Like Malaysia, the colonial rule had shaped the structures of contemporary Indonesian society. The continuous tension between the secular and the Islamist groups in defining Indonesian politics, economic inequality within Indonesia's social stratification, and the existence of dualistic economy in Indonesia are instances of influences generated from the 126 years of the Dutch colonial rule.

[352] Bernard T. Adeney-Risakotta, *Living in a Sacred Cosmos : Indonesia and the Future of Islam* (New Haven, Connecticut Yale University Southeast Asia Studies, 2018).

An imagined community

Indonesia declared its independence from the Dutch colonials in 1945, and after several years of armed and diplomatic conflict with the Netherlands, Indonesia achieved international recognition in 1949. Indonesia is the world's largest island country, with more than thirteen thousand islands, and at 1,9 million square kilometers (735,358 square miles). Indonesia is the 14th largest by land area and the 7th largest in the combined sea and land area. Java, the world's most populous island, contains about 40 percent (100 million) of the country's population.[353] With over 261 million people (2017), Indonesia is the world's fourth-largest nation in the world, the third-largest democracy, and as well as the most populous Muslim-majority country.

Indonesia is a republic with an elected parliament and president. Since its independence, Indonesia has experienced many challenges in establishing a democratic government. After almost a decade of parliamentarian democracy, Soekarno turned it into an authoritarian regime in the final phase of his reign (1959-1965). Then, Soeharto (1966-1998) ruled an authoritarian and repressive regime of the New Order for almost 32 years until the regime fell due to a massive protest in 1998. Since the late 1980s, the Soeharto administration had become heavily centralized and corrupt. When the financial crisis of 1997 started, the crony-capitalism regime of Soeharto was not able to cope with it. The monetary crisis had become a political crisis leading to a democratic transition in Indonesia.

Indonesia is a diverse country. There is no single ethnic, single religion, and single culture that unite this archipelago of 17,000 islands. However, this diverse archipelago is, in fact, a single nation-state. For instance, the people of Sumatra have more differences to people of Java compared to the people of Malaya (Malaysia). Sumatra and Malaya are ethnically Malay, speaking *Bahasa Melayu,* and share many histories as a region. There is no exact reason why the territorial border of Indonesia exists as it is, except because the people themselves believe it to be so.

The Indonesian archipelago has been an essential region for trade since at least the 7th century, but before the Dutch came, Indonesia was only a fiction. In 1914, the Dutch centralized

[353] BBC, "Indonesia Country Profile," BBC, last modified 2 October 2018, accessed 18 April, 2018. https://www.bbc.com/news/world-asia-pacific-14921238.

political control over the whole archipelago after almost a century controlled by a private company of Dutch East India Company or VOC. The Dutch set up a single government for all the Indies, formed a new representative assembly, the Volksraad, and introduced new law codes: a code for foreign Orientals in 1848 and a criminal code for native Indonesians.

This centralization certainly gave a sense of unity in the mind of Dutch administrator, but not in the mind of native Indonesians. None imagined themselves as belonging to an organic, unitary community in any meaningful way. Indeed, the Dutch had a vital role in the creation of a unified Indonesia, but Indonesia exists as a nation mostly because Indonesians themselves want it.[354] The support for this argument is presented in the paragraphs below.

A nation is real for the people who hold it as true, despite the fact that we cannot sense it physically. Benedict Anderson's well-known book, *Imagined Communities*, links the creation of nations, which he called "imagined communities," with the advancement of national languages.[355] Bahasa Indonesia, the national language, was a language of trade, which was spread across the archipelago. It is originated from Malay islands, which is now shared by Indonesia, Malaysia, and Singapore. It is an entirely invented language because we cannot find any ancient texts, which are written in Indonesian. Moreover, there were no native speakers before the twentieth century.[356] Nowadays, Bahasa Indonesia is more consolidated as lingua franca thanks to the national education system, the spread of television, and the popularity of local *sinetrons* or soap operas.[357]

The spread of newspapers among the native Indonesians accelerated this sense of unity. For the first time, these natives spoke, discussed, and shared information as a "one people". Moreover, the second youth congress in Batavia (now Jakarta) in October 1928 marked a milestone in Indonesians' historical conscience. Youth delegates came from various parts of the archipelago to discuss a different array of issues concerning their people. In the final day, the

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[354] Matt Regan, "Imagining Indonesia: A Requiem for Benedict Anderson," (31 January 2016), accessed 23 May 2018, https://publicpolicyindonesia.wordpress.com/2016/01/31/imagining-indonesia-a-requiem-for-benedict-anderson/.
[355] Ibid.
[356]Ibid.
[357] Elizabeth Pisani, *Indonesia, Etc.: Exploring the Improbable Nation*, 1 ed. (New York: W. W. Norton & Company, 2015).

Congress closed with the reading of the Youth Pledge (*Sumpah Pemuda*), which all delegates proclaimed three ideals: one motherland, one nation, and one language. There was no formal decision from the Congress, but it did promote the idea nationhood. The idea of a united Indonesia. [358]

Also, the social stratification created by the Dutch colonialism partly was partly responsible for the creation of this shared identity too. In the nineteenth century, the Dutch consolidated colonial social status system based on racial distinction in the Dutch East Indies (now Indonesia), and particularly in the island of Java. This system created a notion of Bumiputera, which was different, as understood in modern Malaysia. The colonial legal system made an explicit distinction between Europeans, Chinese, and Indonesians. The colonialists put all natives of the Dutch Indies into one big pool of lower-class called Indies or *pribumi* regardless of their ethnicity and religions.

Above them, the Chinese and other 'foreign orientals' such as Arab descent formed an intermediate group consisting mainly of traders and craftsmen, and the one sit on top of the system was the European colonists. This system formed the roots of later ethnic problems. After independence, it continues to create tension between the native and the Chinese Indonesian (1.2 percent of the Indonesian population), particularly in relation to wealth distribution. The Chinese minority population in Indonesia has gained an important position in the business sector with international business networks. Despite this tension, the identity of Bumiputera or *pribumi* in modern Indonesia has never been based on a single ethnic or religious identity.

Indonesia was created based on nationalists' ideals. It is not a nation based on ethnic, race, or religion, but a shared idea of Indonesia. Independent Indonesia transcends the great maritime empires of Indonesia's past from ethnically dominated networks of trade and distance outposts of commerce and religion into a single nation-state.[359] Indonesia is an obvious case of fragmented communities trying to achieve an imagined national unity, as its national motto of *Bhinneka Tunggal Ika*— "Unity in Diversity"—portrays.

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[358]Keith Foulcher, "Sumpah Pemuda: The Making and Meaning of a Symbol of Indonesian Nationhood," *Asian Studies Review* 24, no. 3 (2000).
[359] Regan.

Islam in a religious society

Islam develops not only in a pluralistic, but also a religious vision of the independent and modern Indonesia. Indonesia is the largest Muslim country in the world. There are more Muslims living in Indonesia (215 million) that those who live in the entire Middle East. The growing influence of Indonesian Muslims has been largely ignored by many orientalist scholars or even Arab Muslims. They consider Indonesians practice an inferior form of Islam mixed with non-Islamic indigenous cultural elements.[360]

Indonesia, in fact, is a dynamic Muslim majority country, with incredible diversity. Different streams of Islam, different ethnic groups, and different religious communities, live side by side in harmony. Surely, there were several incidents. The tension mostly happened in the intra-religious relations rather than between religions. The polarization within the Muslim community itself between the modernist, the traditionalist, and the nominal Muslims is very influential in Indonesian politics.[361] This polarization is shown in the debate on Islamic insurance, which will be elaborated in the next section of this dissertation.

Furthermore, Indonesia has experienced several serious terrorist attacks from the extremist Islamic movements and this continuous threat has roots deep in Indonesia’s past.[362] However, this country has also an ancient history of religious tolerance that is far more peaceful than the history of religions in Europe or the Middle East.

The socio-political events in Indonesia are often dominated by religious symbolism of Islam. However, the elections show that Islam plays a smaller part in determining political outcomes. According to Ricklefs, one of the prominent experts on Indonesia, from 1955 to the present, the Muslim political parties have had to adjust to the fact that though Indonesia is overwhelmingly Muslim, the Muslim parties are a political minority. Moreover, he argues, “Islam and religion, in general, serve more or less as ‘social glue’ that keeps society together, peaceful and governable within a society like Indonesia, with weak rule of law, widespread criminality, low

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[360] Kevin W. FOGG, "Seeking Arabs but Looking at Indonesians: Snouck Hurgronje's Arab Lens on the Dutch East Indies," *Journal of Middle Eastern and Islamic Studies (in Asia)* 8, no. 1 (2014).
[361] Adeney-Risakotta.
[362] M. C. Ricklefs, "Islamizing Indonesia: Religion and Politics in Singapore's Giant Neighbour," *Public Lecture* (2004), https://ari.nus.edu.sg/Assets/repository/files/events/ARIPublicLecture-23Sep2004-MCRicklefs.pdf.

levels of administrative competence, endemic corruption and a significant presence of extremist, terrorist groups."[363]

Indonesia is not an Islamic state nor a secular state. Sharia is not the law of the land, with the special exception of the province of Aceh. The Indonesian constitution declared in Chapter XI "The State shall be based upon the belief in the One and Only God, and the State guarantees all persons the freedom of worship, each according to his/her own religion or belief". The belief in the One and Only God is also presented as the first of the five principles of the official philosophical foundation of the Indonesian state (*Pancasila*).

The Constitution establishes the founding principle that the state is religious. This statement means the state has a legitimate role in regulating the religious practice, religious affairs, and for other religious-related civil matters. Unlike Malaysia, that gives supremacy to Islam as the religion of the Federation, Indonesia affirms six religions, including Islam. In order of the size, these are Islam, Protestantism, Catholicism, Hinduism, Buddhism, and Confucianism. All these groups receive state funding, representation in government, publicly funded religious institution, and legal protection. Religious beliefs act as a basis for obtaining legal documents such as identification cards, school registrations, and birth, marriage, or death certificate.[364]

In Indonesia, there are religious courts. There is a Ministry of Religions that regulates religions, not just Islam but others as well. Not only regulating religions, but the state also has the authority to define them. For instance, there is no official law that prohibits Atheism or religious sects in Indonesia. However, as many people consider them as defamation against religion, the government can use the law against blasphemy and defamation to restrict them. The state actor can decide which religious beliefs are normatively acceptable, which ones are deviant, and which ones are a threat to social order.[365] Atheists can be arrested for defamation. The same applies to various sects that are considered heretical versions of one of the six recognized religions. The largest group in this category is Ahmadiya. Ahmadis are not forbidden to practice their version of Islam, but they are banned from teaching or spreading it.

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[363] Ibid.
[364]Adeney-Risakotta.
[365] Ibid.

Furthermore, majority of Indonesians do not imagine their religion as a private matter. They considered religion should affect all areas of life, including politics, economics, social relations, media, culture, family life, and education.[366] Nevertheless, many Indonesian Muslims believe that the substance of Sharia, for example, justice, mercy, and equality, should be implemented in the national law, and Islamic law as implemented from many centuries ago should not be the law of modern Indonesia. This view is not unique only among Indonesian Muslims. Other religious communities in Indonesia share this view also. Adeney-Risakotta states

> Contrary to most of the Malaysian population (64% Muslims) who prefers laws of the country should strictly follow the teaching of the Quran, the majority of Indonesian (91% Muslims) suggests the laws should follow values and principles of Islam, but not strictly follow it. According to many Indonesians, creating a community of justice, safety, and peace is closer to the teachings of the Quran than the purity of Arabic culture. Since Indonesia's founding, there have been repeated attempts to make Sharia mandatory for Muslims. However, most Indonesians has opposed them.[367]

Islam as a political force has always been considered as a threat by the political authority. In 1825, the Dutch had already identified *kiyayi* or village Muslim leaders as their main opponent. They were influential in leading peasant resistance during the Java wars of 1825-1830.[368] Initially, the Dutch tried to curtail Islamic activities and limit the influence of kiyayi by allying itself with local aristocracy and customary chiefs. The contrary, this policy increased the resentment of the Muslim population toward the Dutch. Upon the recommendation of Christiaan Snouck Hurgronje, the Dutch reexamined this policy by distinguishing between the religious and the political aspects of Islam, tolerating the former and repressing the latter. Islamic religious opposition did not shake Dutch rule; however, Islam became more deeply rooted in Indonesian rural society.[369]

The policies of the Soeharto government toward Muslim movements in the 1970s were an echo of those introduced by the Dutch. The Soeharto regime took a strong secular line and coercive approach toward Muslim movements. Not only Muslim political ambition was checked,

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[366] Ibid.
[367] Ibid.
[368] Lapidus.
[369] Ibid.

but also Muslim identities were challenged by nationalist secular ideologies.[370] Islam as an ideology was being disputed against the national philosophical foundation (Pancasila). Islamic organization and association in Indonesia were not allowed to create by-laws using Islam as their organization philosophy. Rather, all organizations had to use Pancasila in their by-laws.

At the beginning of 1980s, the regime began to respond to the rising middle-class commitment to Islam. Soeharto's policy remained the promotion of personal piety and the suppression of political activity, but the government made some concessions, for instance, by building more mosques, schools, reinforcing Muslim courts and banning Christian missionary activity. In the 1990s, the government started to accommodate Islam and acted less repressive toward Muslim movements. Soeharto turned from containment to support for Muslim movements. Soeharto reversed previous policy and created an association for Indonesian Muslim Intellectuals or ICMI to promote the Islamization of Indonesia.[371]

Nowadays, there is no significant opposition either from the government or from society to the deeper Islamization of Indonesia. There is an only difference of opinion about what shape Islamic life.[372] There are some Sharia by-laws, such as the ruling of wearing the headscarf or 'Muslim Clothing' during the fasting month of Ramadan, implemented in the country's more conservative regions. However, most of these regulations have come from officials of ostensibly secular parties like the Golkar or the Demokrat and not Islamist parties. According to Shadi Hamid, the implementation of Sharia is part of a mainstream discourse that cuts across ideological and party lines in Indonesia. That phenomena suggests that Islamism is not necessarily about political Islam but is about a broader population that is open to Islam playing a central role in law and governance.[373]

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[370] Ibid.
[371] M. C. Ricklefs, *Islamisation and Its Opponents in Java: A Political, Social, Cultural and Religious History, C. 1930 to Present* (Singapore: NUS Press, 2012).
[372] Ibid.
[373] Shadi Hamid, *What's Different About Islam in Malaysia and Indonesia?*, vol. 2018, *World Affairs* (The Aspen Institute, 2016).
https://www.brookings.edu/blog/markaz/2016/07/07/whats-different-about-islam-in-malaysia-and-indonesia/

Indonesia's dualistic economy

Unlike the British who laid a solid foundation for a capitalist system in Malaysia, colonialism in Indonesia left out a dualistic system of economy. The dualistic system refers to the coexistent of capitalist and subsistence economies. The character of state-run cultivation crops as a system based on coercion was one of the reasons for the absence of social changes in villages in Java, the island where most of Indonesians live. Despite massive commercialization and machine-intensive colonial economy, village communities were left socially undisturbed. The egalitarian and labor-intensive of village economy had prevailed.[374] In the present day, the dualistic feature is shown by the high level of informal economy in Indonesia. In Indonesia, 70% of the workforce was estimated to be engaged in informal employment, mostly in the agriculture sector.[375] As a comparison, Malaysia's informal workers consists of only around 9.4 percent of the total workforce in Malaysia.[376]

Sir Stamford Raffles introduced a capitalist type of economic development during a brief period when the British took control of Java in 1811. This system was like the one introduced in the Peninsular Malaya. However, when the Dutch returned in 1816, they reverted to direct state control and compulsory cultivation. The Dutch extracted produce, such as coffee and pepper, by forced deliveries for sale in Europe under 'the culture system'.[377]

The culture system was a form of taxation which required by the peasants to devote one-fifth of their land to government assigned crops-usually sugar, indigo, coffee, tea, tobacco, cinnamon, and cotton- and to deliver the produce as a tribute in kind, instead of other rents of taxes. At the same time, the peasants could grow rice for their subsistent need. Also, they were required to contribute their labor: to build irrigation canals, roads, and bridges, clear wastelands, and otherwise build up the economic infrastructure of the island.

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[374] Lapidus.
[375] Carunia Mulya Firdausy, "The Social Impact of Economic Crisis on Employment in Indonesia," *Center for Economic and Development Studies-Indonesian Institute of Sciences* (2000).
[376] Department of Statistics Malaysia, *Informal Sector Work Force Survey Report, Malaysia, 2017* (Kuala Lumpur: 2017).
[377] Lapidus.

During the 1840s, the culture system was overexploited, and could not produce adequate revenues. As the population of Java rose from approximately 7 million in 1850 to 28.4 million in 1900, there was no rise in the per capita standard of living. The culture system had made Java as the vital link in the global capitalist economy, but the peasants in Java were left out within their subsistence farming economy.[378]

After the liberal revolution in Holland in 1848, the state control over plantations and forced labor were abolished in favor of free enterprise and direct taxation. The development of plantation economy, particularly in the island of Sumatra, owed partly to the contract laborers. Many of the contract laborers (coolies) came from China and later from Java. Subsequently, the Chinese played more as an intermediary trader within the colonial economy. They had a vital role in supplying credit and stimulating the cultivation of export crops such as rattan, rubber, and copra.[379]

In Sumatra, the introduction of the capitalist economy led to profound social change. Sumatra became an important source for agricultural and forest commodities. The monetary economy was introduced to create a market for textiles, hardware, and other foreign goods. New towns were established for the new settlers, and Dutch schools were introduced. A network of village banks called the People's Credit System was established. As opposed to Java, capitalism entered the fabric of traditional society to create new classes among the population. [380]

Indonesia's independence had disrupted the continuation of the colonial economy. Although it was not total, the founding fathers of Indonesia envisioned a transformation from the colonial economy. For them, independence does mean not only political independence, but also economic independence, where people are free from exploitation. Their economic ideals were promulgated in the Constitution Chapter XIV. The economic vision of the Constitution is a mixed economy of Indonesia combining egalitarian feature of a cooperative system, state control over major means of production, and private enterprise. Also, the state has a responsibility to take care of the poor and the needy.

[378] Ibid.
[379] Ibid.
[380] Ibid.

Nevertheless, this vision was difficult to achieve during the first decade of independence. After independence, the Indonesian economy had to recover from the hardships of the Japanese occupation and the war for independence (1945-1949). During the period 1949-1965, there was little economic growth, predominantly in the years from 1950 to 1957. In 1958-1965, political instability and inappropriate economic policy measures made the economy stagnant. Soekarno aimed at self-sufficiency, import-substitution, and estranged the suppliers of western capital, even more, when he developed communist sympathies. His efforts to eliminate foreign economic control were not always supportive of the struggling economy of the new sovereign state.[381]

The 'New Order' (Orde Baru) of Soeharto rejected political mobilization and socialist ideology of Soekarno and established a tightly controlled regime. This strategy successfully put Indonesia's economy back on the right track. More flows of foreign investment and foreign aid programs came into the countries. Under Soeharto, Indonesia transformed itself from a predominantly agricultural economy to an industrializing economy.[382]

In the 1980s, Soeharto started to decrease government intervention and initiated the deregulation of the economy. However, this liberalization did not create a more competitive business environment in Indonesia. On the contrary, national companies were sold cheaply to Soeharto families and cronies with the support of a corrupt bureaucracy. Indonesia achieved remarkable economic growth during this time, but it was not distributed to the people of Indonesia. Soeharto regime was sustained by bureaucracy, military, and a small number of conglomerates, which mostly Chinese Indonesian and Soeharto's family. This crony capitalism was responsible for the failure of the Soeharto regime in coping with the financial crisis of 1997.

The economy of Indonesia during the post-New Order is less centralized than the economy during Soeharto regime. Act number 32, the year 2004 serves as a basis for economic decentralization in Indonesia. The region has more autonomy to manage their economic affair. However, the nature of Indonesia economy system does not entirely change. Rosser argues that

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[381] *EH.net*, s.v. "The Economic History of Indonesia," accessed 8 May 2018, https://eh.net/encyclopedia/the-economic-history-of-indonesia/.

[382] Ibid.

Indonesia 'oligarchic capitalism' system has been continually shaped by three contradictory agendas:

> (1) the predatory, rent-seeking agenda pursued by the politico-bureaucrats and their corporate clients; (2) the market-oriented agenda pursued by controllers of mobile capital (and conglomerates when it works to their favors); and (3) the social justice/redistributive agenda pursued by peasants, workers, and small business and their allies in the NGO community. The first two are still dominant in shaping Indonesia economy; however, the political context of Indonesia as democracy creates more space for the third agenda. In general, the current Indonesian economy represents a compromise between these three competing agendas, in particular, the one that favors the interests of the politico-bureaucrats and the conglomerates, while accommodating mobile-capital controllers and incorporating concessions to peasants, workers, and other marginalized elements.[383]

Political actors of Islamic politics

The considerable diversity within Indonesian society is continually changing the political landscape surrounding the development of Islamic insurance in Indonesia. The religious, social and cultural realms are influential in the debate over the role of religion in the country's nation-building and development. Moreover, competition for political power in Indonesia is complex, fought out at multiple levels of government across a nation, in a context of on-going democratization and on-going Islamization of the society. This complex process has a deep root history in the polarization of the Indonesia (Javanese) society which started back in the 1930s. The intensity of the Islamic modernist movement, particularly after the establishment of Muhammadiyah organization in 1912, polarized Indonesian society along identity lines between *santri, abangan* and *priyayi.*[384]

The American sociologist, Clifford Geertz identified three cultural stream or so-called *aliran* in Indonesian, namely the santri, abangan, and priyayi.[385] The abangan majority were not irreligious, for they had a rich spiritual life, but it was only partly touched by reformers regarded as the true Islam. Similarly, the priyayi embraces abangan religious identity but comprises the

[383] Andrew James Rosser, "Indonesia: Oligarchic Capitalism," in *Oxford Handbook on Asian Business System*, ed. Michael A. Witt and Gordon Redding (Oxford University Press, 2014).
[384] Ricklefs, "Islamizing Indonesia: Religion and Politics in Singapore's Giant Neighbour."
[385] Clifford Geertz, *The Religion of Java* (University of Chicago Press, 1976).

elite cultural identity contras to the abangan masses. The priyayi were used as administrators during the Dutch colonial era. Gradually they became professional civil servants of modern Indonesia. For this reason, the priyayi as a class were often regarded as Javanese civil servants.

The santri is a cultural stream of a type of devout Muslim who practice a more orthodox version of Islam, in contrast to abangan classes. The santri consists of the Modernists and the Traditionalists kyais. In term of religious understanding, the Modernists are more puritan by strictly following the injunction of the Quran and early generation of Muslims. Meanwhile, in the context of Muslim society in Indonesia, Traditionalism refers to a religious strand which emphasizes on preserving traditionally established local rituals and scholarship. Traditionalist Muslims refer to themselves as *ahlusunnah wal jamaah* or aswaja.[386]

Furthermore, Traditionalism is often contrasted with modernism, which is inspired by modernity and rationalism. These two groups also differ in many political issues. The Modernist pioneering a modernization of educational and welfare activities. Modernist played roles in nationalist political movements and never shy away from active political involvement and leadership. The Traditionalist started to involve in politics just few years before independence, and continue to do so, however the combination of their religiosity with politics led to questioning of their sanctity. The Traditionalist group tends to be more flexible in their political position, which many suggest pejoratively that the political principle of the Traditionalist is having 'no-principle'. If the religious interest of Muslims is left untouched, the Traditionalists are willing to accept any type of political authority. [387]

The first santri-abangan polarization erupted with the Madiun uprising 1948 which left thousands of dead. With this spilling blood the santri-abangan chasm deepened and reinforced the bitter political contest between the Communist party of PKI and its abangan followers on one side and santri on the other, represented above all by the santri Traditionalist of NU (at that time still within Masyumi). The nationalist party of PNI had a more priyayi leadership but also recruited for abangan.[388]

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[386] Ricklefs, *Islamisation and Its Opponents in Java: A Political, Social, Cultural and Religious History, C. 1930 to Present*.
[387] Ibid.
[388] Ibid.

Under Soekarno, the political landscape was strictly represented this polarization. In the elections of 1955, 'Islamic' and 'secular' constituencies were easily differentiated. The table below shows the vote distribution among the 'big four' parties, who together got 78.0% of the valid votes. This result shows the 'secular' got 38.7% and the 'Islamic' got 39.3%.[389]

During the time of the New Order of Soeharto, the actors and the institutions had changed dramatically. However, the political constellation still showed the polarization between those cultural streams -at least roughly. Also, it had become more difficult to identify 'Islamic' and 'secular constituencies. There was no single organization containing one cultural stream exclusively. There was more political mixing under the New Order. After taking control of the situation in 1965, Soeharto launched an operation to destroy PKI and ensured that the influence of Communism was totally eradicated from Indonesia. Masyumi was already dissolved in 1960 that made Muslim modernist to seek an alternative venue for their aspiration. Although many of former Masyumi members went for Islamic party of PPP for their political aspiration, most of Muslim Modernists preferred non-political institutions (NGOs, press, universities) and focused more *dakwah* or preaching Islam to the society.

The paragraphs below provide a rough sketch of the Indonesia political landscape about Islamic insurance development, particularly under the New Order regime of Soeharto. This serves as a basis for understanding the political landscape behind Islamic insurance development in Indonesia. However, it is important to note that their positions toward Islamization are also constantly evolving and there is often overlap between groups. Their gradual acceptance toward Islamization and Islamic insurance will be discussed thoroughly in the section of Islamic insurance as political identity immediately after this section.

Soeharto regime rested on the support of these three groups: Golkar, Military, and Bureaucracy. Golkar or Golongan Karya (Functional Groups) was founded in 1964 and participated in in the general election for the first time in 1971. Since 1971 Golkar had been the ruling party in Indonesia until 1999. In the 1971 legislative election, Golkar won 62% of the votes and an overwhelming majority in the People's Representative Council (DPR).

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389 M. C. Ricklefs, "'Islamizing Indonesia: Religion and Politics in Singapore's Giant Neighbour' " *Public Lecture* (2004), https://ari.nus.edu.sg/Assets/repository/files/events/ARIPublicLecture-23Sep2004-MCRicklefs.pdf.

Soeharto claimed that Golkar was not a political party. It was portrayed as a non-ideological entity without political that hosted diverse groups in society. It promised to focus on "economic development" and "stability" rather than a specific ideological goal. Golkar also began identifying itself with the government, encouraging civil servants to vote for it as a sign of loyalty to the government. The military or the ABRI was one of the strongest factions under Golkar. Under Soeharto, Members of the Indonesian armed forces played a dominant role in political affairs. The ABRI Commander led this faction in the parliament.

Besides military and bureaucrat, Golkar was also the house for priyayi, abangan, and non-Muslims who were not the loyalist of Soekarno under PDIP, and santri who denounced political Islam (Islamism) under PPP. Although they had different religious understanding, they had a common goal in the eradication of Communism and state control over Islamists. In the early years of the New Order, Soeharto was supportive toward Islamic piety but very repressive on political Islam. However, it started to change in the 1990s when more santri were joining the military and the bureaucrat, particularly Habibie who was recruited by Soeharto to drive the industrialization of the country. In 1978, he was appointed as Minister of Research and Technology. He continued to play an important role in "strategic" industries in this post. By 1991, Habibie oversaw ten state-owned industries including aviation, ship- and train-building, steel, arms, communications, and energy.[390]

Part of the bureaucracy that will be instrumental in the negotiation and implementation of Islamic economy in Indonesia is the Central Bank of Indonesia (BI). BI enables the implementation of Islamic economy within the existing Indonesia economic system.

PDI (Indonesian Democratic Party) was a center-left political party. It was led by Megawati Sukarnoputri, president of Indonesia from 2001 to 2004, and daughter of Sukarno, the first president of Indonesia. Because of its affiliation with Soekarno, the New Order had been maintaining close surveillance and control to the Party. PDI-P was by far the most popular political party coming into the 1999 and the recent 2019 legislative elections.

[390] Ricklefs, *Islamisation and Its Opponents in Java: A Political, Social, Cultural and Religious History, C. 1930 to Present*.

This party has an ideal of the realization of an independent, sovereign, united, democratic, just, prosperous, civilized and religious nation and to fulfill the right and responsibility of all the people of Indonesia. Therefore, it requires the involvement of all national forces, both individually and organized in democratic people's organizations and open to all citizens, regardless of ethnicity, religion, gender, descent and social standing.

Encouraged by the awareness of the responsibility to realize these noble ideals, and to meet the demands of the development of the existing era, the Indonesian National Party (PNI), the Indonesian Christian Party (Parkindo), the Catholic Party, the Supporting Association of Indonesian Independence (IPKI), and Deliberation The Rakyat Banyak (Murba), on March 9, 1970 formed the Development Democracy Group, which was then confirmed by a joint statement by the five political parties on October 28, 1971. And finally, on January 10, 1973, carried out a strategic move to fuse themselves into a forum for people's political struggle based on Pancasila under the name of the Indonesian Democratic Party (PDI). At the close of the PDI II Congress in Jakarta on January 17, 1981, the five fusion parties emphasized that the realization of fusion was complete and stated the termination of their respective existence.

Majority of its member was the priyayi of Soekarno supporters under the nationalist party of PNI and other non-Islamic parties. After the dissolution of the communist party PKI, PDI P has been the main vehicle for abangan, workers, and labors for their political aspiration. PDI P has been a stronghold for the supporter of nationalist ideology based on the official Indonesian national philosophy, Pancasila. PDI P has been positioned as the opponent of Islamism and opposed many of Sharia-inspired laws and regulations.

PPP was formed in 1973 as a result of the merger between several Islam-based parties, assuming the role of umbrella party for Muslims. PPP is considered to be a nationalist Islamist party which conforms to Pancasila doctrine and no longer upholds Sharia as the main goal.

PPP had been the main political vehicle for both santri modernist and santri traditionalist under the New Order. Soeharto forced a merger of political parties following the 1971 Legislative Election. The ten political parties were reduced to just two (excluding Golkar) and that the parties were grouped based on their programs.

The PPP seemed to have cemented itself a status as the strongest opposition party during the Soeharto regime. However, it would not last long. In 1984, Nahdlatul Ulama, under its Chairman, Abdurrahman Wahid withdrew from the PPP and severely weakening it. The PPP was also forced by the government to replace its ideology of Islam with the national ideology of Pancasila and to stop using Islamic symbols. As a result, the party replaced its logo showing the *Kabah* shrine in Mecca with a star.

Nahdlatul Ulama (literally translated to Ulama's Revival, abbreviated as NU) is a traditionalist Sunni Islam movement in Indonesia following the Shafii school of jurisprudence. NU was established on January 31, 1926 in Surabaya as a response to the rise of Wahabism in Saudi Arabia and Islamic modernism in Indonesia. The NU is the largest independent Islamic organization in the world with the membership of 40 million in 2003.

NU has been supportive for the implementation of Sharia principles in Indonesia social and economic development. However, NU is very critical to the strict interpretation of Islam and the stiffness of political position offered by Santri modernists. For instance, on January 2004, the Indonesian Council of Ulama (‘MUI’) issued a fatwa restating the Quranic prohibition on riba or usury and defining that term broadly as any ‘additional charges levied on the postponement of agreed payments’. In April 2010, Muhammadiyah, one of Indonesia’s largest mass Muslim organizations, followed MUI’s lead, issuing a similar fatwa. However, Nahdlatul Ulama (‘NU’), the largest fatwa-issuing organization in Indonesia, and reputedly the largest Islamic organization in the world, sees the matter as *khilāfīya*, that is, subject to different opinions or unresolved. Although many of NU members have become more receptive toward the idea of Islamic economy, they do not have a strict position in term of supporting or abandoning the conventional system. Moreover, many of them still suspect that the modern Islamic financial institution is merely a cosmetic that hinders the profit and political motive of political Islam and does not bring more benefit to the *Ummah* (Muslim community) compared to the existing institutions.

The modernist of Muhammadiyah and Dakwah movements whose base was mainly urban and, in particular, outside Central and East Java-maintained a firmly reformist religious stance with a firmly principled political stance. The modernist agenda was about Islamization from below rather than the imposition of Islamic power from above. This new approach was pioneered

and exemplified by Natsir, a former leader of Islamic party Masyumi, when he created DDII in 1967. [391]

The Modernists are often wary with the increase of Christian missionary activities and the dominance of the Indonesian Christians under the New Order. Therefore, besides confronting Christian missionary activities in the society, their main strategy is infiltrating military and bureaucracy under the New Order. The constant tension between the Modernists and non-Muslims is partly responsible for why the Islamic economy has never received enough support among the non-Muslim in Indonesia.

Another important modernist actor in the late New Order was the *Tarbiyah* movement. This movement was inspired by the global revivalism and to inspiration from the Muslim Brotherhood of Egypt. They were active in campus of public universities. Although they are more conservative in term of observing Islamic religious duties, they are more politically critical toward the Soeharto regime. With freedom of organization and association being severely curtailed, many Indonesian Islamic political activists found inspiration in the Muslim Brotherhood. Collectively, these activists formed what became known as the Tarbiyah (educational) movement.

At the close of the Soeharto dictatorship in 1998, the Tarbiyah had become sufficiently well organized to give rise to Indonesia's main democratic-era Islamic political party, the PK (Justice Party), which became the PKS (Prosperous Justice Party). The members are quite diverse from owners of small or medium businesses, civil servants, to professionals.[392] Many of them become the vital player of the current development of Islamic insurance and Islamic financial institutions in Indonesia.

Indonesian Association of Muslim Intellectuals (ICMI) plays an important role within the political system. Under the patronage of B. J. Habibie, ICMI activists infiltrated the central government. ICMI advocated the domination of Muslims in the ranks of government, civil services, police and military, industries and commerce. ICMI also advocated the introduction of Sharia into the Indonesian legal and political system and oversaw the establishment of Islamic

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[391] Ibid.

[392] Vedi R. Hadiz, *Islamic Populism in Indonesia and the Middle East* (Cambridge University Press, 2016).

courts, an Islamic bank and the promotion of Islamic media. Through ICMI, the modernists established Islamic microfinance (BMT) throughout the country, social relief organization such as *Dompet Dhuafa*, and initiated the establishment of Bank Muamalat and Islamic insurance of Takaful.[393]

MUI (Indonesian Council of Islamic Scholars) is a voluntary forum for ulama or Islamic scholars representing a wide range of Islamic organizations. Although many Indonesians assume MUI is a government agency of some sort, it is an NGO, not a state agency. MUI is endorsed and funded by the government as a key source of state policy on Islamic issues since the 1970s. It enjoys a lucrative state monopoly on halal certification and a revenue stream from the DPS (fatwa body on Islamic economics) system, as well as a significant annual budgetary grant from the Department of Religion. MUI was, in the past, a largely compliant agent of the New Order's repressive, statist and developmentalist policies on Islam.

At the present day, MUI has been able to reinvent itself since Soeharto's fall as a champion of a populist and often 'hardline' conservative orthodoxy that sometimes challenges, but more often leads, government policy. While doing so, it has managed to retain and exploit the aura of state endorsement it has enjoyed since the 1970s, allowing it to remain part of the 'Muslim establishment' of Indonesia — so much so that many Indonesians assume it is a government agency of some sort. In this way, it has become the most influential public advocate of conservative interpretations of Sharia in contemporary Indonesia. [394]

Besides MUI, the supporters of Sharia-based economy established Islamic Economic Society (MES). MES is an intellectual forum serves as an epistemic community in order to disseminate the idea of Sharia-based economy in academia and public at large. At the early days of Islamic banking in Indonesia, the socialization of Islamic Economic was made by each of Islamic financial institutions. After the joint evaluation, it is clear that the socialization of the Islamic economic system can only be successful when done by a structured and continuous manner. [395]

[393] Shofwan Al Banna Choiruzzad, "More Gain, More Pain: The Development of Indonesia's Islamic Economy Movement (1980s-2012)," *Indonesia* 95, no. 1 (2013 2013), https://muse.jhu.edu/article/509626.
[394] Ibid.
[395] Banjaran Surya Indrastomo, "The Emergence of Islamic Economic Movement in Indonesia: A Political Economy Approach," *Kyoto Bulletin of Islamic Area Studies* (2016).

The Islamic financial institutions get together and invite the whole among the required group to form an organization, with joint efforts, will undertake structured and continuous socialization to the society. This organization is called the “Islamic Economic Society” is abbreviated to MES, a reference in the Indonesian language is “*Masyarakat Ekonomi Syariah*, in English, is the Islamic Economic Society or in Arabic is Mujtama’ al-Iqtishad Al Islamiy, established on Monday, 26th March 2001.[396]

MES’ founders are Individual, Financial Institutions, Educational Institutions, Research Institutions and Business Entities which are interested in the efforts to grow the Islamic economy. MES based on Islamic Law, also subject to regulatory legislation that valid in Indonesia, therefore open to every citizen regardless of their religious belief.[397]

The Indonesian government sponsored the establishment of social insurance companies that carry out their activities based on statutory provisions, such as: Perum Jasa Rahardja (now Persero), Perum Taspen, Perum Asabri and Perum Astek (Social Security). With the birth of the New Order regime, the private sector was resuscitated as an important part of the Indonesian insurance industry. And in line with the rapid development in Indonesia, the New Order government carried out development in all fields including insurance. In an effort to discipline and improve the quality of the Insurance Industry in Indonesia, the government has issued various policies in the form of provisions and legislation. Regulations that are important in disciplining the business this insurance field is the Minister of Finance Decree No. 214 and 215 / KMK 013/1988 known as the December Package. Shortly after that a special law was issued regarding insurance business as the first time since the Republic of Indonesia became independent, namely Law No.2 1992 following the Government Regulation No.73 of 1992/KMK/No.223-226 which regulates very detailed the steps of the insurance business.

Indonesian insurance industry consists of five main sectors: life, non-life, reinsurance, civil and armed forces, and social insurance. The civil and armed forces and social insurance are provided by the government. As mentioned before, the constant support of the military and

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[396] Masyrakat Ekonomi Syariah, "Profil," accessed 6 January, 2019. www.ekonomisyariah.org. and also Achmad Mujiharto, “Peranan Islamic Insurance Society Dengan Program Sertifikasi Keahlian Dalam Pengembangan Sdm Asuransi Syariah” (Islamic University Syarif Hidayatullah, 2009).

[397]Mujiharto.

bureaucrats was essential for the New Order regime, therefore the regime prioritized the provision of social insurance for these two groups. Particularly in health care, Indonesian healthcare has traditionally been fragmented: private insurance schemes for those who could afford it, basic state provision for the very poorest, and NGOs in specialized areas providing support in between.[398]

Small number companies dominate the insurance business in Indonesia. The top 10 life insurers from a total of 46 companies control more than 60% shares of total assets and premiums, while the top 10 non-life and reinsurers from a total of 91 companies account for more than 50%. Furthermore, the top two among the five social and civil and armed forces insurance companies account for over 80% of total assets and premiums.[399]

Indonesia's insurance sector has long been open to foreign investment, and while there are calls to restrict engagement by global players, there is no overlooking the fact that the industry needs more funds to meet elevated capital requirements. As local companies get in shape for regional competition in the upcoming ASEAN Economic Community (AEC), the industry is expected to see further consolidation. All of this should open doors for mergers and acquisitions and for foreign firms to enter the market.

During Soeharto, most of the domestic insurance firms were owned or had patronage relationship with Soeharto’s family members. For instance, all insurance contracts from Pertamina, state-owned oil and Gas Company, were subcontracted to a company owned by the youngest son of Soeharto, Tommy. Then, there was a partnership between Bob Hasan and two airlines controlled by Suharto's children. One of business group called the Nusamba group controlled many businesses including insurance.

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[398] Lauren Razavi, "Indonesia's Universal Health Scheme: One Year on, What's the Verdict?," (15 May 2015), accessed 22 April 2018, https://www.google.com/amp/s/amp.theguardian.com/global-development-professionals-network/2015/may/15/indonesias-universal-healthcare-insurance-verdict.

[399] Danan Dito, "Indonesia's Insurance Industry," *Pefindo Articles* (March 2012 2012), accessed 4 April 2019, http://www.pefindo.com/index.php/fileman/file/10.

A growing niche markets

After its establishment in 1994, Islamic insurance in Indonesia has experienced significant growth. Association for Indonesian Islamic Insurance operators (AASI) recorded a high increase in the number of Islamic insurance provider, capital asset, and investment. In 2015, there were more than 60 companies provided Islamic insurance service across Indonesia, which contributed to 5.0% of entire gross written of entire Indonesia insurance industry.[400] With a sizeable Muslim population combined with expected good GDP growth, Indonesia has vast potential growth opportunities for Islamic insurance development.

Indonesians prefer to use the term 'Sharia insurance' rather than 'Islamic insurance'. The usage of 'Sharia' and not 'Islamic' is part of the compromise between Muslim activists and Soeharto regime who considered the term Islamic as more politically subversive within the Indonesian context.[401] However, to avoid any confusion, we keep using the word 'Islamic insurance' in this chapter.

History and development

The development of Islamic insurance only exists in the latter half of 1994. In mid-1993, ICMI (Indonesian Association of Muslim intellectuals) initiated the establishment of the first Islamic insurance company in Indonesia. This initiative was followed up by the formation of the Takaful Indonesia Insurance Team (TEPATI) through a partnership between the Abadi Foundation, Bank Muamalat Indonesia (BMI), and Tugu Mandiri Life Insurance in July 27th, 1993. According to Syakir Sula, Islamic insurance is needed to support the establishment of the Islamic Bank. The establishment of an Indonesian Islamic insurance company in 1994 would protect the fund managed by Bank Muamalat Indonesia, which was founded three years earlier.[402]

Through various national seminars and after conducting studies with Takaful Malaysia on September 1993, finally, TEPATI established PT Syarikat Takaful Indonesia (PT STI) as a Holding

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[400] OJK.
[401] Choiruzzad.
[402] Syakir Sula, interview by Achmad Mujiharto, January 21, 2009, Jakarta, http://repository.uinjkt.ac.id/dspace/bitstream/123456789/19467/1/ACHMAD%20MUJIHARTO-FSH.pdf.

Company on the 24th February 1994. Then PT STI established two subsidiaries, namely PT Asuransi Takaful Family Insurance (ATK) and PT Takaful General Insurance (ATU). The birth of Islamic insurance in Indonesia is mainly the result of the commitment of the Takaful Insurance Indonesia (TEPATI). Furthermore, it was also the fruit of various elements of initiative, namely the Association of Indonesian Association of Muslim Intellectuals (ICMI) through the Abdi Bangsa Foundation, Bank Muamalat Indonesia Tbk, PT Tugu Mandiri Life Insurance, Ministry of Finance of the Republic of Indonesia, Indonesian Muslim entrepreneurs, with technical assistance from Syarikat Takaful Malaysia Bhd. (STMB).

The two Islamic insurance companies were established based on Malaysia's Islamic insurance model. PT Takaful Family (ATK) Insurance inaugurated through Minister of Finance Decree No. Kep-385 / KMK.017 /1994. It was opened by Mr. Mar'ie Muhammad as the Minister of Finance at that time on 4 August 1994 with 5 billion IDR initial investment. This company provides life and other family Takaful services. PT Takaful General Insurance (ATU), established later 2 June 1995, offers general Takaful services.[403]

The role of these two Indonesia's Islamic insurance companies in the country's economy through sharia-based insurance has attracted domestic and foreign investors. In 1997, Syarikat Takaful Malaysia, Bhd. (STMB) places its capital in the company to become one of the shareholders. STMB then increased the amount of its capital investment to reach a significant amount in 2004. The role of Syarikat Takaful Malaysia Bhd. (STMB) as an investor continued through direct capital participation in PT Takaful Family (ATK) in 2009. The Islamic Development Bank (IDB) also strengthened the company's capital structure in 2004. Domestic investors also showed a keen interest in participating in developing Takaful Indonesia. In 2000, *Permodalan Nasional Madani Persero* (PNM) helped strengthen the company's capital structure. Internally, PT. General Takaful Insurance standardizes to improve and maintain the consistency of service quality and company performance through the application of ISO 9001: 2008, which is the latest international standard for the quality management system.

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[403] Abdullah Amrin, *Meraih Berkah Melalui Asuransi Syariah: Ditinjau Dari Perbandingan Dengan Asuransi Konvensional* (Jakarta: PT Elex Media Komputindo, 2011).

The establishment of these two companies has also motivated others to establish a new Islamic insurance company or open Islamic insurance window or division. Many Islamic insurance companies were established particularly after the year 2000. Asuransi Syariah Mubarakah (1997), PT Jaya Proteksi Takaful (2010), and PT Maskapai Asuransi Sonwelis (2015) were set up as new family Takaful insurance companies. This type of insurance provides life, education fund, and investment services like Takaful Family in Malaysia. Meanwhile, PT MAA Life Assurance (2000), PT MAA General Assurance (2000), PT Great Eastern Life Indonesia (2001), PT Asuransi Tri Pakarta (2002), PT AJB Bumiputera 1912 (2004), and PT Asuransi Jiwa Bringin Life Sejahtera (2003) were established as window or Sharia-unit. Global insurance companies were also interested in this new financial service. PT Asuransi Allianz Life Indonesia (2006) and PT Prudential Life Assurance (2010) are some examples of global companies that open Islamic insurance businesses in Indonesia. Compared to other countries, Indonesia is well known for having many Islamic insurance operator in its jurisdiction.

According to the law, there are four methods of establishing an Islamic insurance company in Indonesia. The first method is by founding a new Islamic insurance company. The second method is through conversion from a conventional insurance company into an Islamic insurance company. The third method is by having a new Islamic insurance unit or window. The fourth method is through the conversion of conventional insurance unit or window into an Islamic insurance unit of window. Based on the latest OJK database (2018) on the Islamic insurance company, there are currently 19 units/windows and five full-fledged Life/Family insurance companies, 25 general Islamic insurance windows, three full-fledged general Islamic insurance companies, and three reinsurance companies in Indonesia.[404]

However, not all companies perform well. After operating for more than two decades, PT Asuransi Syariah Mubarakah was filed bankruptcy in court by Indonesia Financial Service Authority (OJK). PT Takaful General Insurance (ATU), the pioneer of Indonesia Islamic insurance, was closed at the beginning of 2017 because of lack of premium growth. However, PT Koperasi Simpan Pinjam Jasa (Kospin Jasa), one of the biggest credit unions in Indonesia, bought the ATU

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[404] The Financial Service Authority (OJK), *list of Islamic insurance company in Indonesia.* accessed November 7, 2018. https://www.ojk.go.id/id/kanal/iknb/berita-dan-kegiatan/publikasi/Pages/Daftar-Perusahaan-Asuransi-Umum,-Jiwa-dan-Reasuransi-dengan-Prinsip-Syariah.aspx

majority share in 2018 and revitalized it. Other companies are being merged to or acquired by other more prominent companies. Tokio Marine Group, a global insurance company originating from Japan, made an acquisition of MAA Life Assurance in 2012. PT Jaya Proteksi Takaful changed its name into PT Asuransi Chubb Syariah after being acquired by the US-based company, Chubb Corp in 2017. Other company such as PT Asuransi Tri Pakarta, a small company with an asset less than 200 billion IDR (13 million USD), thrives and becomes one of the best units of Islamic insurance companies.

The new law No. 40 the year 2014 (UU40 2014) gives incentive for the spin-off of Islamic insurance windows (i.e., the split of Islamic insurance units from the conventional insurance companies into a separate standalone entity) within the framework of ten years. This regulation is expected to spur market activity. However, most of the existing companies have not enough Islamic insurance business to meet the immediate separation condition. Some companies may choose to make use of the full 10 years to plan for the spin-off as required by the UU40 2014. Meanwhile other companies may adopt a strategy of an early spin-off to gain the first-mover advantage.[405]

In 2016, Islamic insurance in Indonesia contributed to 6.2 percent of the total insurance industry in Indonesia. In number, there was 2,168 billion IDR (145.3 million USD) of life & family Islamic insurance premium and 585 billion IDR (39.2 million USD) of general Islamic insurance and reinsurance. It was 10.25% growth from the previous year. The increase in asset and investment were much better. The asset of Islamic insurance grew about 21.69 percent, and the investment reached 23.64 percent growth. The total asset of Islamic insurance was 28,967 billion IDR (1.9 billion USD), and the total investment of Islamic insurance was 25,726 billion IDR (1.7 billion USD). The increase in motor vehicle leasing contributed significantly for the premium of general Islamic insurance. Meanwhile, life insurance had not increased dramatically because of the economic recession during that year.[406]

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[405]Milliman, *Global Takaful Report 2017: Market Trends in Family and General Takaful*. http://www.milliman.com/uploadedFiles/insight/2017/Takaful-2017-full-report.pdf and Yudi Suharso, "UU No 40 Perasuransian Diharapkan Angkat Industri Asuransi Syariah," (27 May 2015), accessed 7 February 2019, http://keuangansyariah.mysharing.co/cat/keuangan-syariah/.

[406] AASI, "Data Bisnis Asuransi Dan Reasuransi Syariah Aasi Q1 2016," accessed. https://www.aasi.or.id/.

The top three of life/family Islamic insurance players are Prudential Life Assurance, AIA Financial, and Asuransi Allianz Life Indonesia, all of which operated via windows. These companies make up a market share of more than 70% in 2015 for the life/family Islamic insurance industry in Indonesia in terms of total contributions/premiums. Based on the Financial Services Authority (OJK) report, a large proportion of the new business by these top three operators are on unit-linked products. A unit-linked insurance plan is a product offered by insurance companies that, unlike a pure insurance policy, gives members both insurance and investment under a single integrated plan. This model has been a significant factor driving the growth in the Indonesian life/family Islamic insurance sector. [407]

The key distribution channel in this market is predominantly agency.[408] Companies are also using the existing banking networks as a more efficient means of distribution. However, Islamic banking in Indonesia is small compared with conventional banks in terms of assets. Islamic insurance has been more successful when there is a Bancassurance partnership with conventional banks. For instance, AIA has a long cooperation with the Bank of Central Asia (BCA) for both conventional and Islamic insurance segments. For this reason, AIA has increased its market significantly from 2% in 2010 to 24% in 2014 in terms of total contributions.

The top three players for general Takaful or Islamic insurance sector are Asuransi Astra Buana, Asuransi Takaful Umum, and Asuransi Adira Dinamika. These companies make up around 50% of the market share for general Islamic insurance in Indonesia. The key lines businesses of general Islamic insurance in Indonesia are motor, personal accident, health, and property. For general Islamic insurance in Indonesia, the retail business lines are predominantly sold via agency force, and the commercial business lines are predominantly sold via brokers.[409]

The development of Islamic insurance elaborated above is a result of the rise of Muslim activism since the 1980s. Although the official establishment of Islamic insurance company did not start before 1994, the idea of Islamic insurance can be traced a few years back before that. It is more suitable to use the term Islamic economic movement in Indonesia preferably than

[407] Milliman 2017.
[408] Islamic Finance News, *What Does the Future Hold for the Takaful Industry in Indonesia?* (islamicfinancenews.com, 2014).
[409] Mlliman 2017.

Islamic finance project as commonly known in Malaysia. It is because the initiative came from the periphery of the power, instead from the state. Muslim intellectuals, universities, religious organizations, and Islamic NGOs played a more important role than the government in developing ideals of Islamic economy. Adding to that, the term Islamic economy or economics is also more common to use in Indonesia compared to term Islamic finance. It is because the idea of Islamic economics is regarded to encompass broader aspects than mere finance by many Indonesian intellectuals and activists.

The 1980s was a difficult time for Muslim activists in Indonesia. Any alternative ideas such as Islamic economy was considered subversive toward the state's development agenda. For that reason, it was not possible to implement the concept of Islamic economics into formal institutions. In the 1990s, Soeharto regime changed its policy toward Muslim group. This decade was also a crucial period for the implementation of Islamic economics in Indonesia. The Bank Muamalat Indonesia established in1991 as the first Islamic bank in the country.

Majelis Ulama Indonesia (MUI, Indonesian Council of Islamic Scholars) and ICMI played a crucial role in this development. In the 1990s, both organizations were rising as meaningful representations of Muslim groups in their relationship with the state. Initially, Soeharto approved the establishment of these organization to appease and gain support from the Muslim population. Both organizations were also enjoying the patronage of the Soeharto regime. Several religious decrees of fatwas were issued to support the Soeharto developmental agenda, for instance, fatwa on contraception for supporting national family planning program and fatwa justifying state-sponsored sports lottery. [410]

In the late 1980s, the situation changed. Rather than an instrument of the state to influence and control the Muslim population, it was transformed into a canal of aspiration for Muslim groups to influence government policies.[411] In 1989, Amin Aziz, one of the leading pioneers of Islamic economy movement and also a MUI member, introduced an initiative of establishing an Islamic bank. MUI then organized a series of workshop to discuss interest and

[410]Shofwan Al Banna Choiruzzad, "More Gain, More Pain: The Development of Indonesia's Islamic Economy Movement (1980s-2012)." Indonesia 95, no. 1 (2013): 125-72.
[411] Ibid.

banking in Islamic perspective (18- 20 August 1990), which eventually led to the establishment of Bank Muamalat Indonesia in 1991.[412]

On October 30th, 1992, the government issued Government Regulation No. 72/1992 on Profit-sharing Based Bank. The Indonesian Central Bank (BI) supported this development by issuing the operational guidance for Profit-sharing-based Banks with the BI Circular Letter No.25/4/BPPP on February 29th, 1993. Furthermore, the BI team sent personnel to Singapore, London, New York and Iran to learn about the practices of Islamic banking and finance.[413] Many initiatives were launched in this period. Many of these initiatives were conducted as MUI or ICMI programs. Discussions and experiments by Islamic economy movement activists also resulted in the establishment of two Islamic insurance companies in 1992 and hundreds of Sharia microfinance of *Baitul Maal wat Tamwil* (BMT).

After Soeharto regime collapsed in 1998, Islamic economic institutions have been growing more rapidly. There has been a stronger attachment between Islamic activists, intellectual and universities, politicians, and state bureaucrats on the idea of the Islamic economy. Moreover, the historical role of MUI in the establishment of Islamic financial institutions made its prominence in the governance of the Islamic economy industry is unquestionable. In 1999, the National Sharia Council of MUI (DSN-MUI), was born with the MUI Decision No. Kp. 754/MUI/II/1999. Furthermore, DSN-MUI is accepted as a significant authority in the governance of Islamic banking and finance, even though DSN-MUI is not a governmental institution. Based on DSN-MUI fatwas, the Central Bank (BI) issues regulations on Islamic-related finance, which are legally binding.[414]

From 2000 until 2010, DSN-MUI has already issued 78 fatwas related to the Islamic economy industry.[415] On January 24th, 2004, MUI formally issued a fatwa on the prohibition of interest, Fatwa MUI No. 1 the year 2004 strongly declared that the current practices of interest are clearly matched with the definition of usury. As a result, the Islamic economy has become an integral part of Indonesia economy. Moreover, DSN-MUI has become the primary actor in the operation of the Islamic economy in Indonesia. There was no public resistance against the

[412] Ibid.
[413] Shofwan Al Banna Choiruzzad, "The Central Bank in the Development of Islamic Economy Project in Indonesia: Role, Motivations and Moderating Effect," *立命館国際研究* 25, no. 2 (2012/10 2012).
[414] Ibid.
[415] Ibid.

development of Islamic financial institutions in Indonesia, and more Islamic insurance companies, and governmental task forces or committees were established to support Islamic finance development in Indonesia.[416]

Regulatory framework

Currently, Insurance Law number 40/2014 (UU40 2014) regulates both Islamic insurance and insurance companies in Indonesia. UU40 2014 covers the aspect of corporate governance, market conduct, consumer protection, and licensing of insurance industry in Indonesia. Indonesia does not regulate Islamic insurance separately from conventional insurance. The Indonesian Financial Service Authority (OJK) collaborates with the religious institution, the Indonesia Council of Islamic Scholars (DSN-MUI), to enforce the Sharia compliance within the industry. Both institutions have different tasks. On one hand, the Indonesian Financial Authority (OJK) sets the minimum capital requirement, the solvency regulation, policyholder protection, and foreign ownership restrictions to protect the industry. On the other hand, DSN-MUI provides guidance and evaluates the implementation of Sharia in the insurance contract and practice. The purpose of the adoption of UU40 2014 is to boost Islamic insurance business expansion, and at the same time, to ensure the standard of Sharia-compliant of the service.[417]

Before Law No. 40 of 2014, the growth of Islamic insurance was supported by regulatory provisions that guarantee certainty sharia insurance law. Legal provisions governing insurance sharia, among others: First, Law No. 2 of 1992 concerning Business Insurance. Secondly, Government Regulation No. 73 of 1992 concerning Implementation Insurance Business, as amended by Regulation Government No. 63 of 1992. Third, Decree of the Minister of Finance Number: 421 / KMK.06 / 2003 September 30, 2003, concerning Capability Assessment and Compliance for Directors and Commissioners of Insurance Companies. Fourth, Minister of Finance Decree Number: 422 / KMK.06 / 2003 September 30, 2003, concerning Managing Businesses of Insurance Companies and Companies Reinsurance. Fifth, Minister of Finance Decree Number: 423 / KMK.06 / 2003 dated September 30, 2003 concerning Inspection of an

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[416] Ibid.
[417] Milliman, *Global Takaful Report 2017: Market Trends in Family and General Takaful*.

Insurance Company. Sixth, Decree of the Minister of Finance Number: 424 / KMK.06 / 2003 dated 30 September 2003 concerning Financial Health of Insurance Companies and Companies Reinsurance. Seventh, Decree of the Minister of Finance Number: 426 / KMK.06 /2003 dated September 30, 2003 concerning Business Licensing of Insurance Companies and Reinsurance Company. [418]

Law No. 2 of 1992 and other regulations mentioned above on insurance before UU40 2014 did not correctly regulate Islamic insurance. In the Code of Commerce Law Article 246, namely: "Insurance is an agreement where someone is responsible tie yourself to an insured by accepting something premium, to provide compensation to him for a loss, damage or loss of possible expected benefits he will suffer because of an uncertain event." That definition could not be used as a legal basis for Islamic Insurance. The definition does not regulate the existence of insurance based on Sharia principles and does not regulate technical implementation insurance activities. Therefore, guidelines to run an Islamic insurance business was established in the Fatwa Council National Sharia Insurance Indonesian Ulama Council (DSN-MUI) No.21 / DSN-MUI / X / 2001 concerning General Guidelines for Islamic Insurance.[419]

DSN-MUI is a non-state institution and has no legal force because it is not included in the laws and regulations in Indonesia. DSN-MUI is different from the National Sharia Advisory Council (NSAC) of Malaysia. The NSAC, which was established on May 1, 1997, functions as the highest authority in deciding Sharia matters in Islamic financial institutions bank or nonbank. NSAC is in the organizational structure of the Central Bank of Malaysia (BNM). Member NSAC was appointed by the board of directors of BNM for a three-year working period and can be re-elected in the next period.[420]

There are some legislations to give stronger legal certainty of Islamic insurance in Indonesia. Those regulations are the Decree Minister of Finance of the Republic of Indonesia No. 426 / KMK.06 / 2003, Ministerial Decree RI Finance No. 424 / KMK.06 / 2003 and Decree of the Directorate General Financial Institution No. 4499 / LK / 2000 and finally, the Regulation Government No. 39 of 2008.

[418] Maksum.
[419] Ibid.
[420] Rudnyckyj.

Also, the issuance of Law Number 3 the Year 2006 concerning Amendments to Law Number 7 of 1989 regarding Religious Courts, which in their provisions give authority to the Religious Court to handle sharia business disputes. In the event of a commercial dispute between customers and the company, there are three ways to solve it according to Indonesian law. First, peaceful settlement among the parties. Second, the parties choose facilities dispute resolution in the form of arbitrage and alternative dispute resolution. This arrangement is set in Law Number 30 of 1999 about Arbitrate and Alternative Settlement Disputes or called *tahkim*. Third, dispute resolution through court, which in this case is through a religious court. [421]

Since the development of the Islamic economic finance industry, it becomes a necessity to have specific authority to examine, hear, decide and complete the case. On this basis, a Law No: 3 was issued in 2006 stating that the Religious Courts has authority to examine, try, decide and resolve cases in the field Sharia Economy. The Decision of the Constitutional Court No. 93 / PUU / X / 2012 was also added, which states that the Religious Courts have absolute authority in examining, adjudicating, deciding and resolving cases Islamic economics is pursued through court, then the Court.[422]

The new insurance law of 2014 favors full-fledged Islamic insurance entities, instead of window operations. The purpose is to stimulate growth and competitiveness of the Indonesian Sharia insurance industry in the longer term. Insurance companies are likely to focus on boosting their Sharia businesses, and gradually enhancing their capacity and capitalization to achieve the maturity needed to finally be independent of their conventional units.[423] Also, article 1 Number 8 of the Insurance Law UU40 year 2014 regulates the risk management business based on Sharia Principles in order to help and protect all participants against losses.[424]

Furthermore, Islamic insurance and Islamic Reinsurance businesses are regulated differently from conventional insurance and conventional reinsurance businesses. Insurance business and conventionally managed Reinsurance Businesses apply the concept of risk transfer, while Islamic insurance and Islamic Reinsurance Businesses are the application of the risk sharing

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[421] Daod Wan Norhayate Wan et al., *A Comparative Analysis on Takaful Acts between Malaysia and Indonesia*, *1st Aceh Global Conference (AGC 2018)* (Atlantis Press, 2019).

[422] Ibid.

[423] Bashar Al Natoor, Global Head of Islamic Finance, Fitch.

[424] *Undang-Undang Republik Indonesia Nomor 40 Tahun 2014 Tentang Perasuransian*, vol. 40 (2014).

concept. Considering the different conceptions underlying the business operation, the Islamic insurance business and Sharia Reinsurance Business will be encouraged to be held by separate entities from the conventional entities.[425]

The article 54, Law No. 40 of 2014 regulates the obligation of Insurance Companies, Sharia Insurance Companies, reinsurance companies, and sharia-reinsurance companies. One of the obligations is the requirement of each Sharia Insurance Companies, reinsurance companies, and sharia reinsurance companies to be members of mediation institutions.[426]

Furthermore, the article 57-67 of the Insurance Law describes the authority that can be carried out by the Financial Services Authority so-called OJK. OJK is the primary institution to regulate and supervise Insurance business activities. The regulation and supervision include aspects of governance, business behavior and health finance. What is meant by "supervision" includes analysis of reports, checks and investigations.

There is also ruling for the obligation of every insurance company related to insurance business association. According to article 68, each Insurance Company to be obliged to become a member of one of the Insurance Business Associations by the type of business. This arrangement is intended to enhance the role of associations in regulating its members (self-regulatory). It is also to facilitate better coordination with the Financial Services Authority.[427]

Compared to Malaysia's IFSA 2013, UU40 2014 referring to Islamic insurance company and conventional insurance company in Indonesia was simpler and only discuss on the headlines for insurance and Islamic insurance. The further explanation of it will be provided in the *Peraturan Otaritas Jasa Keuangan (POJK)* or Indonesia Financial Authority. On the contrary, IFSA 2013 totally referred to Islamic insurance covered all the Islamic insurance rules and regulations and compiled of banking, Islamic insurance and money market. [428]

Indonesia regulates Islamic insurance together with conventional insurance. Although the new regulation gives more detail rulings on Islamic insurance compared to the previous regulations, the Law does not give detail instruction on Sharia transactions. The Law gives more

[425] Suharso.
[426] "Undang-Undang Republik Indonesia Nomor 40 Tahun 2014 Tentang Perasuransian."
[427] Maksum.
[428] Wan Norhayate Wan et al.

role to DSN-MUI to guide and monitor the implementation. Therefore, the DSN-MUI Fatwa Institution is considered to be the highest Sharia authority holder in Indonesia. The National Sharia Council (DSN) is an institution formed by the Ulama Council Indonesia (MUI) which has the function of carrying out the tasks of the MUI in handling issues related to the activities of sharia financial institutions. One of the main tasks of the DSN is to study, explore and formulate values and principles of Sharia (Islamic Law) in the form of fatwas (legal opinion of Islamic scholars) to be used as guidelines in activities transactions in Islamic financial institutions.[429] Through the Sharia Supervisory Board, supervision of the application of Sharia principles in the system and management of the Islamic financial institution. However, DSN-MUI is not a governmental institution, therefore, its fatwas (legal opinions) are not legally binding. The fatwas must be sustained by the decree from the relevant governmental agency.

Although Indonesia regulates Islamic insurance within the same regulatory framework of conventional insurance, Indonesia gives more role to the religious or Sharia court. It is the religious court who has the authority to settle a dispute concerning Islamic insurance in Indonesia. This is quite different from Malaysia that gives that authority to civil court.[430]

Islamic insurance companies in Indonesia were developed based on the Malaysian model. Therefore, we cannot see much differences between the two countries in the way Islamic insurance company operates. However, Indonesia has a different regulatory framework from Malaysia. Indonesia acknowledges the existence of Islamic insurance as part of Indonesia economy and does not intervene on the detail of the Sharia rulings. The Indonesian state limits itself from being a direct participant and acts purely as a regulatory body, and not even as an incubator of Islamic insurance like Malaysia.

Special features and challenges

The lack of centralization effort by the Indonesian government creates a shortage of skills in the Islamic insurance industry, particularly in risk management, actuarial and underwriting

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[429] Tim Lindsey, "Monopolising Islam: The Indonesian Ulama Council and State Regulation of the 'Islamic Economy'," *Bulletin of Indonesian Economic Studies* 48, no. 2 (2012), http://dx.doi.org/10.1080/00074918.2012.694157.

[430] Wan Norhayate Wan et al.

expertise. The education on Islamic insurance is mostly conducted by study groups in universities, Islamic NGOs, and the Islamic insurance agencies themselves. The role of insurance agents or marketers is vital in the implementation of Islamic insurance in society. Agents act as an intermediary between Islamic insurance companies with the community. Moreover, an Islamic insurance agent has several roles beside as influential marketers of Islamic insurance products. The agent has a role in providing access to information, guarding the excellent image of Islamic insurance companies, and providing solutions and services to prospective customers as well as insight to the public on Islamic insurance. [431]

Islamic insurance in Indonesia has a distribution challenge given the large geographical spread. This issue is not only resulted in term of lack of resources but also a huge gap on public awareness of Islamic insurance as a financial tool. Many companies who have Islamic insurance window dedicate more resources on the conventional product rather than Islamic insurance.[432]

However, the lack of government support and skilled human resources motivated Islamic insurance companies to be more innovative in their unit-linked products. Unit-linked products enable investors to get both insurance and investment under a single integrated plan. Malaysia has been a pioneer in the Family Takaful plan, whereas members can invest in their children's education fund and at the same time, receive insurance protection. Islamic insurance companies in Indonesia copied and extended this model. Not only education plan, but members can also invest in social investment such as *Waqf* (social endowment) or other religious obligation such as Hajj. Waqf is not private investment, but it is an endowment made by a Muslim to a religious, educational, or charitable cause. Rather than investment for the college entrance fee, Muslim can invest in building a mosque, school, or hospital.

In 2017, PT Sun Life Financial Indonesia ("Sun Life") launched a *Waqf* feature for an insurance policy of Sharia life insurance products. This feature will not only allow Sun Life to offer a solution for better financial planning and protection but also fulfill the needs of clients to serve religious obligation, particularly in doing a Waqf.[433] In order to do so, members can utilize the

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[431] Edi Hariyadi and Abdi Triyanto, "Peran Agen Asuransi Syariah Dalam Meningkatkan Pemahaman Masyarakat Tentang Asuransi Syariah," *Jurnal Ekonomi dan Perbankan Syariah* 5, no. 1 (2017).
[432] Milliman Takaful report 2017.
[433] Sun Life, "Sun Life Financial Indonesia Launches Waqf Feature for Shariah Insurance Product," Sunlife.co.id, last modified August, accessed 27 June, 2019.

benefit of their insurance and investment. CIMB Malaysia adopted this model in 2018 by introducing product named Takaful Mulia.

Some Islamic health insurance plan covers not only the costs of medical treatment but also the costs of alternative medicine, which is any of a range of medical therapies that are not regarded as orthodox by the medical profession, such as herbalism, homeopathy, acupuncture, and Islamic prophetic medicine.[434] The later refers to the actions and words (hadiths) specifically of the Prophet Muhammad with regards to sickness, treatment and hygiene, and the genre of writings undertaken primarily by non-physician scholars to collect and explicate these traditions.[435]

Furthermore, Indonesian Islamic insurance companies work together with Islamic NGOs to deliver their products to the consumer. Norman Nugraha, Chief Agency Officer Shariah Sun Life says that the company intends to assist Muslims in Indonesia participating in social program. Therefore, all investment returns of Islamic life insurance at Sun Life is changeable to waqf or social endowment, such as school, health clinic, or mosque. Moreover, the clients can choose any authorized waqf institution of which is Sun Life's partner, such as Indonesian Waqf Board (*Badan Wakaf Indonesia or BWI*), Dompet Dhuafa, Rumah Waqf, and registered institution in Indonesian Waqf Board.[436]

Accommodating Islamic insurance

Malaysia and Indonesia are experiencing different result related to the development of Islamic insurance. The birth of Islamic insurance in Indonesia is attributed to the Indonesian Muslims activism of the late 1970s. The initiative was not coming from the center of the state power but from peripheral Muslims who demanded alternative economic platform to the failing state's economic policy. According to these Muslim activists, Soeharto regime was able to

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https://www.sunlife.co.id/ID/About+us/Newsroom/Press+releases/2017/Sun+Life+Financial+Indonesia+Launches+Waqf+Feature+for+Shariah+Insurance+Product?vgnLocale=en_CA.

[434] Eric Iskandarsyah, "Asuransi Syariah Dinilai Jadi Pilihan Tepat Semua Kalangan," *Republika*2017, https://republika.co.id/berita/ekonomi/syariah-ekonomi/17/08/17/outsro-asuransi-syariah-dinilai-jadi-pilihan-tepat-semua-kalangan.

[435] Muzaffar Iqbal, *Science and Islam* (CT: Greenwood Press, 2007).59

[436] SunLife.

maintain a constant economic growth, however, it excluded part of the population from gaining its benefits. They considered Soeharto's economic policies had increased inequality of income distribution between the people and between regions.

Furthermore, economic liberalization under Soeharto had made Indonesia bound to the power of foreign capital. International institutions such as the IMF and the World Bank had been dominant forces in determining economic policies under Soeharto. Islamic insurance and other Islamic financial schemes in Indonesia were born out of criticism toward the economic policies of the New Order regime.

The absence of direct government involvement and the lack of political support for Islamic insurance and Islamic financial institutions, in general, are the causes behind this slow development. Besides the competitive insurance structure of Indonesia, Indonesian State does not fully support Islamic insurance because it sees and treats it as a 'political identity' of a particular social group within a pluralistic Indonesia that needs to be accommodated and compensated, rather than a vital tool for national economic development. The deepening of Islamization within the contemporary Indonesian society makes the state not to ignore or even reject Islamic financial institutions. At the same time, any attempt to push the state beyond its current role as a regulator of Islamic insurance will create resistance not only from the non-Muslim population but also from the Muslims of different cultural streams. The following sections present this argument thoroughly.

The birth of a resistance

The 'New Order' (*Orde Baru*) of Soeharto adopted a military method of dealing with political-economic problems faced by Indonesia. Soeharto rejected political mobilization and socialist ideology of Soekarno and established a tightly controlled regime that stabilized politics for economic growth. Contrast to the previous regime, Soeharto encouraged trade and foreign investment in Indonesia. Moreover, Soeharto since the 1970s boosted the capital intensive of oil and mining industries, so that the country's income from oil and gas increased from $ 0.6 billion in 1973 to $ 10.6 billion in 1980, which has a value equal to 80% of Indonesia's exports. Under Soeharto leadership, Indonesia was able to be self-sufficient (in term of rice production) in the

1980s and had maintained economic growth 6% -7% per year. Also, Soeharto successfully reduced the national poverty level from 60% in 1970 to 17.74% in 1996.[437]

Nevertheless, many critics suggested that the reliance of Soeharto's economic policies in oil and gas industries and economic liberalization had made Indonesia dependent on the power of foreign capital. Furthermore, as economic growth had been the priority, economic distribution had been neglected by the Soeharto regime. For over three decades (1966-1998), Soeharto implemented a socio-economic strategy based on the development trilogy: high economic growth, political stability, and equity. The policy goals of growth and stability were met by and large, but many experts indicate the income inequality increased rapidly under Soeharto, as well as the share of the labor force engaged in informal sector activities.[438]

The inequality was exacerbated by the lack of social protection for Indonesians. Compared to Soekarno, Soeharto had invested significantly in providing nation-wide health services through primary health centers, known as *Puskesmas*. However, the centers provided access to health only at the most basic level. Also, many of them did not have any insurance protection. The state provided insurance only to civil servants and military personnel, while most of Indonesian live their live without any formal financial protection arrangement. In his attempts to restore stability to the nation, Soeharto relied very heavily on the military and the highly centralized, Javanese civil service. Health insurance for these two groups and their families was expanded significantly in 1968; it grew into a program eventually named Askes that had 17.5 million members by 2003.[439]

Combination of political control and economic liberalization at the beginning of Soeharto’s administration is not unique. It was commonly practiced by leaders in the East and Southeast Asia regions. Strict leadership style was considered vital to fix the messy economy in the late 1960s. This choice gave political consequences. All political forces, press, and NGOs

[437] Ewout Frankema and Daan Marks, *Was It Really "Growth with Equity" under Soeharto? A Theil Analysis of Indonesian Income Inequality, 1961-2002* (Groningen: Groningen Growth and Development Center, University of Groningen, 2007).
[438] Ibid.
[439] Elizabeth Pisani, Maarten Olivier Kok, and Kharisma Nugroho, "Indonesia's Road to Universal Health Coverage: A Political Journey," *Health Policy and Planning* (2016).

opposed to the New Order were then given no space. Moreover, the New Order regime was very repressive to these alternate voices, particularly toward Islamic movements.

The global euphoria of the success of the Iranian Revolution of 1979 resonated well with Islamic movements in Indonesia. Although it was a Shia revolution, it did not prevent many Muslim intellectuals and activists in Indonesia to take inspiration from that. Prior to the Iranian Revolution, there was already an explosion of the *usroh* movement, which is initiated by Hasan al-Banna of the Egyptian Muslim Brotherhood, on Indonesian college campuses in the late 1970s and early 1980s.

The success of the Iranian Revolution provided a psychological boost for Muslim activists particularly in mosques around campuses. Muslim women activists in Indonesia especially college students, were struck and awakened by the women of Iran who dressed traditional garment but managed to repel the domination and influence of the superpower United States from their country. The Iranian Revolution has become a powerful inspiration for the affirmation of self-esteem, confidence and a new identity for the *dakwah* (missionary) activists. It started from the image of Iranian women in their hijab then spread through the campus mosque network in Indonesia and extend its influence on all walks of life.[440]

However, Soeharto continued his policy that dates back since the beginning of the 1970s to allow religious expression of Islam but not political Islam. In reality, the line between individual piety and political expression often blur. Wearing hijab is an individual choice, but in public space, it can be seen as an expression of a political identity. Soeharto regime did not allow public school students to wear hijab (headscarf) in school and any official photo identification. Soeharto's government further his political control over civil organizations by declaring in 1984 that henceforth only Pancasila and not Islam or any other religion or ideology, could serve as the ideological basis for mass organizations in Indonesia.

These socio-political circumstances forced the aspiration for Islamization including ideas of Islamic economy to be confined within campuses walls. Intellectuals and students studied the work of modern Muslim intellectuals including the work by prominent Shia cleric Muhammad

[440] Moeflich Hasbullah, *Islam Dan Transformasi Masyarakat Nusantara: Kajian Sosiologis Sejarah Indonesia* (Jakarta: PrenadaMedia, 2017).

Baqir Sadr: *Our Economy (Arabic: "Iqtisaduna").* Written between 1960 and 1961, and published in 1982, *Our Economy* still forms much of the basis for modern Islamic banking. In his book, al-Sadr shows that Islam has answers to problems of the modern world by presenting an Islamic alternative to both capitalism and socialism.[441] He rejects socialism and capitalism by arguing both private and public property originate from God, and that the rights and obligations of both private individuals and rulers are therefore dictated by Islam.

Not only from Iranian intellectuals, but Indonesia Muslims have also been developing ideas of Islamic economy other international economist such as who writes a series of books titled *Islamic economic doctrine*. In the book, the insurance model from an Islamic point of view is thoroughly explored. He argued that the practice of commercial insurance is not permitted by Islam. Also, he also contends that life insurance that makes the soul as an object of insurance is not in accordance with Islamic law. Aside from conventional insurance based on insurance practices in Europe, it also contains elements that are prohibited by Sharia.[442] Other book *Insurance in Islam* by M. Nejatullah ash-Shiddiqie explains the risks, the nature of insurance and the bad things related to insurance. In addition, insurance in the capitalist, socialist and Islamic systems is discussed and argued for the supremacy of Islamic insurance.[443] From these works, Indonesian Muslim intellectuals developed insurance plans adjusted for Indonesians.

The pioneers of the Islamic economic movement, among others A.M Saefuddin, Dawam Raharjo, Adi Sasono and Amin Aziz, came from intellectual background of Pusat Pengembangan Agribisnis (Centre of Agribusiness development), Bogor Agricultural Institute.[444] This center was established in 1982 as an intellectual forum focusing on a wide array of economic issues, including the idea of Islamic economy. Besides organizing conferences, several experiments on Islamic financial institutions were implemented. In 1984, Bandung Institute of Technology students found a Sharia microfinance called *Baitut-Tamwil* Teknosa. [445]

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[441] Baqr as-Sadr, *Our Economics* (WOFIS, 1994).
[442] Afzalurrahman, *Doktrin Ekonomi Islam*, trans. Suroyo and M. Nastangin (Yogyakarta: PT. Dana Bhakti Wakaf, 1996).
[443] M. Nejatullah ash-Shiddiqie, *Asuransi Di Dalam Islam*, trans. Ta'lim Musafir (Bandung: Penerbit Pustaka, 1987).
[444]Choiruzzad.
[445] Ibid.

In his book titled *Nilai-Nilai Ekonomi Islam* or the Principles of Islamic Economics published in 1984, AM Saefuddin mentions specifically Islamic insurance together with Zakat, Islamic Banking, and Waqf (social endowment) as instruments to implement the principles of Islamic economics.[446] According to Saefuddin, there are three fundamental principles of Islamic economics: the optimum benefits of property ownership, moderation, and justice. Islam teaches that property should be utilized to bring benefits not only to individuals but also public at large. There is no concept of absolute ownership in Islam. Private and public property ownerships are acknowledged only when it is utilized to achieve that goal and remove any exploitation from one toward the others.

Moreover, Islam also teaches Muslims to live in moderation, parsimony and avoid extravagance. Lastly, the principle of justice means that economy should bring benefit to all people and not particular individuals or groups within the society. Justice can be achieved both through a market and a non-market mechanism. Zakat and other forms of charity are used when individuals or groups cannot access economic benefit through market mechanism.

Although Islam does not oppose the market mechanism and private sector, Islam regulates how business is conducted. The prohibition of usury is to ensure that there is no exploitation resulted from any business transaction. For this reason, Saefuddin advocates the establishment of Islamic Bank and Islamic insurance in Indonesia. Saefuddin argues that conventional banking and insurance ensure profit only to one party and leave another party with a higher risk of the business. Islamic insurance or Sharia insurance is based on mutual help so that people can share the burden and risk when one of them is facing economic difficulties. In sum, AM Saefuddin emphasizes the importance of economic activities to be grounded in religious values. The economy is not only a pursuit of profit, but it is also an activity toward ethical life.

However, the 1980s was a difficult time for Muslim activists in Indonesia. Despite this development, the impact and scale of the Islamic economy project were still very minimal. The banking regulation (1967 Law on Banking) did not give any room for the establishment of any noninterest banking institution. The state was not supportive towards the idea of Islamic

[446] A.M. Saefuddin, *Studi Nilai-Nilai Sistem Ekonomi Islam* (Jakarta: Media Da'wah, 1984).

economy, which was considered subversive toward state's development agenda. For that reason, it was not possible to implement the approaches of Islamic economics into a formal institution.[447]

In the 1990s, Soeharto regime changed its policy toward Muslim group. This change was also an important period for the implementation of Islamic economics in Indonesia. The Bank Muamalat Indonesia established in1991 as the first Islamic bank in the country, and later, PT Syarikat Takaful Indonesia (PT STI) was established in 1994 as the first Islamic insurance company in Indonesia. The following paragraphs elaborate on the process of how these Islamic economics activists negotiate with the state and try to find space within the existing system.

State as the regulator of Islamic insurance

Ever since taking office in 1967, President Soeharto committed to undertake the revitalization of Indonesia's economy. Beyond his rhetoric of creating a just-and-equitably-prosperous society in a material and spiritual sense based on Pancasila, Soeharto adopted the Western capitalist development model. the New Order recruited neo-classic economists mostly graduating from American universities, especially the University of California, Berkeley.[448]

Minister of Finance, J.B. Sumarlin who was in office in 1988 until 1993, did not object the establishment of Islamic banks, because according to him, it did not contradict the Indonesian Constitution. The government started to accommodate the idea of Islamic economy. Choiruzzad documents this transformation in the government's stand in more detail.

> Several organizations established Islamic banks in the form of *baitul mal* (financing house) had been set up such as the Co-operative for Professional Services (*Kooperasi Jasa Keahlian*) Teknosa Bandung in Bandung on 4 July 1984 and Koperasi Ridho Gusti in Jakarta. The Organization of Islamic Conference (OIC), especially with its Islamic Development Bank (IDB) greatly contributed to further development of Islamic banks in Indonesia. On June 1990, Minister for Foreign Affairs, Ali Alatas, inaugurated the Jakarta OIC Economic Consultative Forum, to promote economic relations between Indonesian and other members of the OIC. On 19 March 1991 Minister of Home Affairs Rudini and Minister On 19 March 1991 Minister of Home Affairs Rudini and Minister of Religious Affairs Munawir Sjadzali signed a joint decree on the development of the Islamic

[447] Indrastomo.
[448] *EH.net*.

Almsgiving Management Body (Badan Amil Zakat, Infaq, dan Shadaqah, BAZIS) which is a non-governmental organization, but worked under the government's supervision. [449]

Moreover, the Indonesian Council of Ulama (MUI) was given task preparing the establishment of an Islamic bank without interest, the Bank Muamalat Indonesia (BMI). Soeharto promised an interest free loan from his Foundation of the Pancasila Muslim Action (Yayasan Amal Bhakti Muslim Pancasila) of the IRP 3 milliards. In addition, several Muslim big entrepreneurs, including Fadel Muhammad, Aburizal Bakrie, and Fahmi Idris, were interested in the creation of Islamic banks. The government's support for the BMI suggests that Soeharto regime recognized the need to acknowledge the Muslim community in a more practical manner and to bring them into national, economic development.[450]

Soeharto personally donated 50 million rupiah and 3 billion rupiah from the Foundation Amal Bakti Amal Pancasila which he led. In addition, there are 9 largest shareholders of the Bank Islam, all of which are individuals or offshore foundations, Bob Hasan (figure corporate) worth 25 billion rupiah, GLC 4.5 billion, Krakatau Steel 3.5 billion, Hutomo Mandala Putra 3,3 billion, Pensiun Nusantara Foundation 3 billion, Pertamina 2 billion, Aburizal Bakrie 2 billion, Ibrahim Rasyid 2 billion and YDBKS 2 billion.[451]

If in Malaysia, the largest accumulation of capital and bank owners is government institutions and state Islamic departments, in Indonesia Islamic bank ownership originated from private sector, social organizations and individuals known closely with Soeharto. This situation explains several things. First, Soeharto's approach uses those close to it as a stock owner the largest bank signals that Soeharto has more to act as individual rather than as a President. This means, though has the power to issue policies and regulations based on the constitution existing, but Soeharto does not use the state allocation for injection bank capital. Secondly, as it further emphasizes individual decisions, Soeharto wants to say that formally, the state is not involved in the Islamization process which is quite vibrant. In addition to the question that Soeharto needs to take care of not feeling Islam and avoid criticism of the existence of the bank, it can be seen

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[449] Choiruzzad.

[450] Muhamad Ali, "Islam and Economic Development in New Order's Indonesia (1967-1998)" (paper presented at the East-West Center International Graduate Student Conference Series, Honolulu, 19-21 February, 2004).

[451] "Bank with Trust Fund," *Tempo*, 9 November, 1991.

as Soeharto's consistent stance on Pancasila's ideology confirms Indonesia not as an Islamic and not a secular state.[452] In the late 1980s, President Soeharto started to question the loyalty of top military leaders. Following the increasing distrust toward military, Suharto went closer to Muslim groups.

However, the predatory environment of widespread corruption within Soeharto regime gave dilemma for the proponents of Islamic economics. On the one hand, they need support from the state, but on the other hand, they need to ensure that Islamic financial institutions were built independently and be consistent with the moral goals of Islamic economics.[453]

Based on several experimentations and surveys, the Central Bank (BI) came into a view that rather than a threat to the conventional system, Islamic finance could play a supportive role to strengthen the existing national economic system. BI requested the participation of many Islamic economy activists in the process of developing the regulatory environment for Islamic banking in Indonesia. [454]

BI expected that this non-interest-based banking would be able to reach out a certain part of the population who see interest as usury and thus forbidden by the religion. More choices of financial services mean wider mobilization of public fund. [455] Islamic economics, according to BI, is not to replace the existing banking system, but instead to strengthen it.

Seeing BI’s positive response, some Islamic economy activists were becoming more and more moderate. Some started to think the possibility of the ‘coexistence’ of Islamic economic within the existing system. On the other hand, many of BI officials were also becoming more supportive towards Islamic economy movement.[456]

However, despite the convergence of interests, there was also continuing tensions, in which the state and Islamic economy movement negotiate the role of the state in the Islamic banking and finance. Choiruzzad describes this negotiation process, which led to a compromise

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[452] Fadlilllah Amin, “Perjuangan Penubuhan Negara Islam Dalam Era Kebangkitan Islam Di Malaysia Dan Indonesia, 1982-2004” (Thesis (PhD), University of Malaya, 2017), http://studentsrepo.um.edu.my/id/eprint/7540.
[453] Choiruzzad.
[454] Ibid.
[455] Ibid.
[456] Ibid.

on the role of BI as representative of the state and DSN-MUI as the representative of the community withing the architecture of Indonesia's Islamic economy.

> During the legislation process of the 2008 Islamic Bank Law, BI wanted to establish Islamic banking committee (KPS) within the BI structure with significant power to regulate the Islamic banking industry. In the KPS, BI promised to fairly accommodate representatives from the business, Islamic religious scholars, and Islamic economists. This idea was not completely accepted by business actors due to their worries that BI will have stronger control to the industry and thus limiting its growth. MUI was also not really fond of the idea because it worried that the KPS will take over their role (for example: to issue fatwa regarding Islamic banking practices). Finally, the KPS was established under BI structure, but with an unclear role, more like an advisory board, and not as powerful as it was designed. The power to issue fatwa stayed in DSN-MUI (*Dewan Syariah Nasional Majelis Ulama Indonesia*, Indonesia Islamic Scholars Council's National Council of Sharia). However, because MUI is not a state body, it has no legal power. Thus, as before, the fatwa only serves as an accepted agreement among the actors and only become a legal rule after BI issued a BI regulation (*Peraturan Bank Indonesia*) based on that fatwa.[457]

Later, BI transferred the authority of managing financial services to the Financial Services Authority of Indonesia (OJK). At the end of 2011, as an effort to reform the financial sector, the government and the House of Representatives (DPR) agreed to establish OJK. Then, on November 22, 2012, Law No. 21 concerning OJK was ratified. This so-called independent institution will function from December 31, 2012, which replaces the functions, duties and regulatory authorities that have been carried out by the Ministry of Finance through the Capital Market and Financial Institution Supervisory Agency (*Bapepam-LK*). Then at the end of 2013, the turn of functions, duties and authority for banking regulation and supervision by Bank Indonesia (BI) would also be transferred to OJK.

A political accommodation in a multi-cultural society

The moderation and stabilization effects provided by Indonesian state through its financial authorities has created a new challenge for the supporter of Islamic banking and insurance in Indonesia. Now, the Islamic financial services have been accepted as a private-based insurance service within the existing national economy. It enables diverse players to be involved

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[457] Ibid.

including the multinational insurance companies. Although the insurance law no 40/2014 gives permission for cooperatives to establish Islamic insurance, most of Islamic insurance providers are insurance companies. ICMI, MES, MUI, insurance companies, and Indonesian financial authorities are becoming the vital actors for Islamic insurance development and their dominance has raised criticism, including from the pioneer of Islamic economics themselves. The Muslim Brotherhood-inspired of political party of PKS clearly states in its platform that Islamic economy should be an integral part of Indonesia economic development. Indonesian state should take active role to expand market share and gradually transfer its dependence on international donors toward self-sufficient and international Sharia-based financing.

Furthermore, Islamic banking and insurance as accommodating capitalism later become ideological barrier for many center-left politics (Muslim and non-Muslims) to support the establishment of these institutions. According to Dawam Rahardjo, as stated in the book *Islamic Economic Architecture* (2015), Islamic economics is currently still considered too focused on the discourse on finance and banking with sharia trademarks.[458] The presence of Islamic finance or Islamic banks is indeed a symbol of Islamic economic revival. In the 21st century, perceptions of the rise of the Islamic economy are arguably rising significantly. This was triggered by great interest and curiosity in Western countries.

However, there is a dilemma in the development of the Islamic finance industry. Among these are capital requirements, because most sources of capital come from foreign or non-Muslim capital. In addition, Islamic banks and insurance also tend to adopt conventional banking and insurance techniques and loosen the basic principles of Sharia law. This is done because in order to be competitive, Islamic financial institutions must glance at large projects that are high in risk.

For this reason, the Islamic economic system should ideally be developed with institutional economic epistemology. With epistemology, the concept of an Islamic economy that is operational is no longer limited to the financial sector. The Quran illustrates that the usury institution must be replaced with the *zakat* and *tijarah* institutions. While the Hadith or prophetic tradition also regulates the existence of waqf institutions that are directly related to the real

[458] Dawam Rahardjo, *Arsitektur Ekonomi Islam* (Bandung: Mizan, 2015).

economic sector. According to Dawam, zakat and waqf are actually instruments to solve poverty problems. Unfortunately, the practice of Islamic economics is still limited to the financial sector, so the essence of Islamic economics as an institutional economy has still not been achieved.[459]

Other argue that Islamic economy should not be determined by a certain label. An important principle of a sound economic system is a system that does not contrary to moral values and does not impair the humanitarian value such as the existence of exploitation and injustice. It is a system that encourage competition in doing good deeds or *fastabiqul khairat*. According to this view, Islamic economy can be named anything as long as it is consistent with the moral values of the economy.

The modernist organization of Muhammadiyah has been slowly embraced this private-based Islamic insurance. Before the establishment of the first Islamic insurance in Indonesia, on April 27, 1992, the Muhammadiyah sought cooperation with a conventional insurance company, PT Asuransi Jiwasraya. The cooperation was aimed to realize the program of economic development for Muslims, particularly the members of Muhammadiyah.[460]

The Muhammadiyah considers conventional insurance is haram, however it can be accepted when it gives more benefit to individual and society.[461] Therefore, according to Muhammadiyah social insurance provided by the state, such as Taspen, Askes, and insurance for social and religious reasons, such as insurance for hajj and education are not a violation against Islamic law.

Historically, the Muhammadiyah prefers to manage the organization fund by itself. However, due to lack of expertise and resources in managing insurance business, recently the Muhammadiyah has made several agreements to work together with Islamic insurance company. For instance, Muhammadiyah of West Java (DPW Jabar) signed a memorandum of understanding (MoU) with Recapital Life Insurance (Relife) in the Islamic insurance participation program for Muhammadiyah residents.

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[459] Ibid.
[460] Arie Lukihardianti, "Umat Islam Belum Pahami Konsep Asuransi Syariah," *republika.co.id*, 22 February, 2015, https://www.republika.co.id/berita/ekonomi/syariah-ekonomi/15/02/22/nk5owp-umat-islam-belum-pahami-konsep-asuransi-syariah
[461] Majlis Tarjih, *Keputusan Majlis Tarjih Muktamar 1987* (Malang: Muhammadiyah, 1987).

Like the Muhammadiyah, the Muslim Traditionalists NU, which today claimed to have some 35 million members, had already carried out local economic activities since its establishment. The NU already discussed the permissibility of bank interest in the first forum in 1927. The campaign of Islamic economics starting from early 1980s brought this topic to be a public issue. In 1982, forum in Bandar Lampung once again brought the issue of bank interest and even touched upon the issue of Islamic bank. Again, there was no single agreement. As in 1927, there were three different views on the issue of interest: the view that interest is usury and thus it is prohibited (haram), the view that interest is not usury and thus it is allowed (halal), and the view that it is in doubt (*shubhat*) because of the existence of different views.[462] However, there were also differences within the first camp. Within the first camp, which argued that interest is prohibited, there were differences between those who argued that interest is prohibited at all situation and those who argued that despite its haram status, interest is allowed due to the emergency until a bank which operates according to Islamic existed. Despite these differences, the idea of Islamic banking was generally considered positive among NU circles in 1980s.

Abdurrahman Wahid, the grandson of the organization's founder and the leader of this new generation of NU was very critical on the Islamic economics project, particularly when it is supported by the state. After he took the leadership of NU in 1984, his enmity toward modernist groups had put the organization against the establishment of Islamic banking and insurance.

Wahid strongly criticized ICMI's initiative on the establishment of Indonesia's first Islamic bank. He said ICMI as willing to sacrifice the security of depositors' fund just to comply with "an outdated tenet of Islamic scriptures." He then described Islamic financial institutions as a'moral burden for Muslims", arguing that "it is hard to imagine a financial vehicle more vulnerable to abuse". Wahid saw the initiative, backed by ICMI, was part of the agenda of Political Islam. When Bank Muamalat Indonesia was finally established in 1991, he commented that it was "another victory for those who want to see Islam as a political alternative." [463]

[462] Indrastomo.
[463] Ibid.

The NU mostly suspicious with the motive of the Muslim Modernists, and not with the idea of prohibition of interest itself. Instead of supporting the Islamic economy project, the NU opened a People's Credit Bank (Bank Perkreditan Rakyat, BPR) in 1990 by cooperating with the Summa Bank, a bank owned by a Catholic family, to establish some 2,000 BPRs. The Summa Bank would provide staff, financial share and training. It was hoped that the NU could contribute to economic growth especially in rural areas. Abdurrahman Wahid explained that there was nothing prohibited in the economic field to cooperate with people from other religions if they are capable and honest.[464]

PDI-P shared the view of Abdurrahman Wahid of seeing Islamic finance and insurance as a mean for political Islam. However, as more Muslims and elite santri joined PDI-P, this party has become more responsive and less strict toward the aspiration of the Muslim population. 50% of PDI-P constituent are Muslim, and they are mostly the middle and poor of the Muslim population. According to PDI-P, Indonesia should develop its economic system according to Indonesian characteristic based on cooperation. PDI-P does not voice open opposition against the Islamic economy; however, it still sees the Islamic economy as a foreign product and gives benefit only to a small group of the society. PDI-P is very critical not on the religious aspect of the Islamic economy but how the idea is implemented according to the Constitution and other regulations. PDI-P promotes a middle ground between Islam and pluralistic Indonesia.[465]

Furthermore, as the santri Modernists and Traditionalists are debating the legitimation of Islamic banking and insurance within Indonesia's economy, PDI-P which mostly represents the abangan cultural stream and non-Muslim were advocating for a universal social security system for all Indonesian. Suharto's downfall and the subsequent elections led to the euphoric embrace of the concept of citizens' rights on the part of Indonesians who had heard about nothing other than their responsibilities for more than three decades.

In 1999, in the first truly democratic elections in nearly 45 years, Indonesians favored the PDI-P party led by Megawati Sukarnoputri, which had campaigned on a platform of increased equity. The following year, the new parliament amended the 1945 constitution to include the

[464] Ibid.
[465] Idris Thaha, *Islam Dan Pdi Perjuangan: Akomodasi Aspirasi Politik Umat* (Gramedia, 2018).

"right to receive medical services". Two years later, a further constitutional amendment specified that the state was responsible for ensuring health service provision, as well as for developing a social security system for all citizens. The next clause, reminiscent of the declaration of independence, stated that the details would be worked out later. PDI-P leader Megawati, then Vice-President, set about working out the details. An unwieldy working group of over 60 people drafted a social security law that, in its first version, envisaged the fusion of all four state-owned insurance firms into a single entity, which would operate as a single payer, not-for-profit trust fund. Minutes of meetings and interview accounts show that this was hotly contested, not least by the existing insurance firms and those who benefited from the profits they generated.

Besides being reluctant to lose their cash cows, directors of state firms were reportedly concerned that the restructuring would open their books to public scrutiny. Employers were afraid that the plan would raise costs, partly because they could no longer opt out of the state-run scheme. They argued that the mandatory schemes violated human rights. Private sector employees and some labor unions also opposed the draft bill, because under the new structure, workers would have to contribute to premiums formerly covered entirely by employers. What's more, they worried that premiums paid by workers and employers would be used to subsidize services for the poor and unwaged, leading to a cut in benefits for those in work. Advisors favoring private sector interests, including from the United States, objected to the fact that the state would have a virtual monopoly on provision of social insurance. [466]

The bill was reportedly revised 56 times before a draft was submitted to parliament in January 2004. In 2014, Indonesia embarked on an exciting and ambitious strategy to move towards universal health coverage through *Jaminan Kesehatan Nasional* (JKN), the country's single-payer national health insurance scheme. The Government of Indonesia spends significant resources to cover membership costs for the poor and near poor under JKN administered by BPJS, which stands for B*adan Penyelenggara Jaminan Sosial* (Social Insurance Administration Organization).

In conclusion, the development of Islamic insurance in Indonesia was influenced by the global Islamic revivalism of the 1980s, political repression by Soeharto regime, and economic

[466] Pisani, Kok, and Nugroho.

deprivation experienced by many Indonesians. Compared to Malaysia's experience, Indonesian Muslims have been emphasizing not only the un-Islamic practice of the conventional insurance in term of violation of Sharia ruling but also how this un-Islamic practice led to socio-economic problems of foreign domination, political disenfranchisement and economic deprivation of the Muslims. From the perspective of Soeharto economic policies, the idea of Islamic insurance and Islamic finance in general came from the 'wrong side' of Indonesia political spectrum. It came as a criticism toward the ruling regime of Soeharto, and only the change in the political attitude of Soeharto toward Islam and the political environment in the 1990s had made the idea of Islamic finance eventually took off.

At the height of harsh authoritarian rule of the Soeharto era, Islamic political activism was often the focus of the most intense of state repression. Because the Indonesian Communist Party had been destroyed in the 1960s, only Islamic organizations possessed the potential to mobilize substantial grassroots support. Thus, they were considered a threat to the centralized and rigid authoritarianism of Soeharto's New Order regime. However, as Soeharto experimenting totalitarianism by controlling Islamic affairs, the Islamist had become closer to Soeharto and endorse Islamization, including Islamic insurance from inside the system. Moreover, alongside the rapid expansion of the economic liberalization under Soeharto, the society witnessed the emergence of Non-Government Organizations (NGOs) involved in the penetration of Islamic economic concept and practices in the public sphere.

However, this unique quality of the movement had never reached significant progress until complemented by the unexpected reorganization of the environmental setting of the political economy of the nation in the 1990s. Soeharto became more accommodative toward Islamic movement, particularly on the idea of Islamic or Sharia economics. As a result, Islamic financial institutions had started to gain legitimacy and support to co-exist with the conventional institutions and practices. These institutions take a role in capital and resource distribution, particularly in the poor rural and urban areas.[467]

This political accommodation continues after the New Order regime of Soeharto collapsed in 1998. The government issued more regulations to support the development of

[467] Indrastomo.

Islamic financial institutions. Islamic insurance has become a legitimate scheme to fill the gap left out by the government's social insurance and conventional insurance schemes.

The introduction of Islamic banking and insurance within the public domain of the national economy has created another problem. Choiruzzad identifies continuing tensions could, in which the state and Islamic economy movement negotiate the role of the state in the Islamic banking and finance.[468]

Indonesian state has taken the role as regulator of Islamic banking and insurance. The state limits itself from any direct involvement in funding or even acts as incubator like Malaysia. The slow development of Islamic insurance in Indonesia can be attributed to this choice. Also, Indonesia has not been a good regulator either. Many experts argue that the rampant condition of corruption during the New Order and the post-Soeharto era has dampened the development of Indonesia's economy in general.

Furthermore, the democratization of Indonesia's socio-politico and socio-economic arena in the post-Soeharto era has imposed a change to the environmental setting of the Islamic economy. Instead of creating a regime-supportive setting like Sudan, Kuwait, and Malaysia, democratization in Indonesia generates a free contested market with extended and market-based development likewise the case of Jordan and Turkey.[469] Now, Islamic insurance companies must compete not only with conventional insurance companies whose service has become more available, but also with the provincial and state-funded social insurance schemes. There is less incentive for Indonesian Muslims to choose private-based Islamic insurance over other schemes. As a result, with the largest Muslim population in the world, the development of Islamic insurance in Indonesia seems to be running in the place.[470]

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[468] Choiruzzad.

[469] Baskan, 2004; Malley, 2004

[470] Minister of National Development Planning (PPN) / Head of the National Development Planning Agency (Bappenas) Bambang Brodjonegoro considers that the development of Islamic economics in Indonesia tends to run in place Bambang while delivering a speech at Indonesia's High Level Discussion: Center for World Islamic Economics, at the Bappenas Office, Jakarta, Wednesday (25 / 7/2018). This article has been aired on Kompas.com with the title "Bappenas: Development of Indonesian Sharia Economy on the Road", Ridwan Aji Pitoko, "Bappenas: Development of Indonesian Sharia Economy on the Road," (25 July 2018), https://ekonomi.kompas.com/read/2018/07/25/170000126/bappenas.

The absence of direct government involvement and the lack of political support for Islamic insurance and Islamic financial institutions, in general, are the causes behind this slow development. Indonesian State does not fully support Islamic insurance like Malaysia because it sees and treats it as a 'political identity' of a particular social group within a pluralistic Indonesia that needs to be accommodated and compensated, rather than a vital tool for national economic development.

The deepening of Islamization within the contemporary Indonesian society makes the state not to ignore or even reject Islamic financial institutions. At the same time, any attempt to push the state beyond its current role as a regulator of Islamic insurance will create resistance not only from the non-Muslim population, but also from the Muslims of different cultural streams.

Islamic banking and insurance have been accepted by the political communities in Indonesia. Islam has penetrated the dominant nationalist, secular and Pancasila based political parties and has made them stronger in their contest against Islamic parties, which are no longer the lone channel for Islamic aspirations. Tanuwidjaja argues that the fact that almost all parties have accommodated religious aspirations and shied away from criticizing controversial religious issues shows the strength of religious influence in the contemporary Indonesian politics.[471]

However, it does not mean that there is a single agenda of 'Islamic economy' agreed across the board. For the modernists, the current practice of Islamic economy finance is primarily a vehicle through which to call attention to a unique Muslim identity. The pioneers of Islamic economy in Indonesia appeared to identify strongly with the idea that Islamic finance offers more equitable means of distributing wealth than conventional finance. While for many, 'Islamic economy' should not be interpreted exclusively with a particular label. Moreover, they have criticized continuously the current implementation of Islamic banking and insurance which according to them, Islamic banking and insurance only provide an improvement to the exploitative system of capitalism, instead of altering it. [472]

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[471] Sunny Tanuwidjaja, "Political Islam and Islamic Parties in Indonesia: Critically Assessing the Evidence of Islam's Political Decline," *Contemporary Southeast Asia: A Journal of International and Strategic Affairs* 32, no. 1 (2010).
[472] See Islamic finance as identity in Karen Hunt-Ahmed, *Contemporary Islamic Finance: Innovations, Applications, and Best Practices* (John Wiley & Sons, Inc., 2013).

Civil Islam and the critical attitude towards Islamic insurance

This section discusses the ‘social life of Islamic insurance’ meaning how Islamic insurance as a commodity is accommodated as a social practice within Indonesian society. It elaborates the redefinitions of Islamic economic beliefs and meanings that have shaped Indonesian understanding of entrepreneurship and human agency. The NEP and economic development in Malaysia created a new Malay entrepreneur class that is very receptive toward the private-based institution of Islamic economy. Moreover, the processes produce and emplace Islamic norms, ethics, hierarchies, practices, and gendered identities enacted in corporate life.[473] There have been different processes happened in Indonesia that lead to a different trajectory of Islamic insurance development in Indonesia.

The amalgamation of rich precedents of a communal economy, economic exclusion and foreign domination, and state repression by the New Order regime generate Islamic reform movement that emphasizes civil institutions and the communal economic ethics. Rather than creating vibrant Muslim entrepreneurs but with conservative mindset like in Malaysia, the Civil Islam of Indonesia, as Robert Hefner define it, repudiated the goal of the Islamic state, mobilized religiously ecumenical support, promoted women's rights, championed democratic ideals, and advocate an indigenous and egalitarian economy. As a result, the current practice of private-based Islamic insurance does not receive wide support among Indonesian Muslims.[474]

This section consists of two parts. The first part provides empirical finding on how Islamic insurance is presented by companies, agents, and religious organizations and how people respond to it. The second part contains discussion on the emergence of Civil Islam identity under the New Order regime and explains how this identity strengthens and reshapes the existing communal economic ethics within Indonesian society. The ethics determine how Indonesians, particularly the Muslims, perceive risk, economic insecurity, and how Islamic insurance can or cannot be the tool for solving those challenges.

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[473] Sloane-White, Patricia. *Corporate Islam: Sharia and the Modern Workplace*, Cambridge University Press, 2017. ProQuest Ebook Central, http://ebookcentral.proquest.com/lib/odu/detail.action?docID=4812344.
Created from odu on 2018-10-03 10:01:05.

[474] Robert W. Hefner, *Civil Islam: Muslim and Democratization in Indonesia* (Princeton University Press, 2000).

Islamic insurance Vis a Vis 'serve without self-interest'

The following section elaborates in detail how Islamic insurance is presented within Indonesian society and how they respond to it. Islamic insurance transcends Muslim understanding of risk and provides the non-usurious way to respond to it. However, as Indonesian Muslims become more pious and accept the prohibition of 'interest' practiced by the conventional insurance companies, they still have an objection with the 'self-interest' motive of Islamic insurance companies. It is hard to accept by majority Indonesian Muslims that a mutual help of bearing each other burden is managed through a private scheme. I argue that this is the main 'social factor' of the slow development of Islamic insurance in Indonesia.

As Indonesians become wealthier due to economic modernization and more pious due to the deepen Islamization process within Indonesian society, the traditional ideals of surrender, acceptance, and gratitude toward tragedies are indeed being evaluated. The idea of making financial preparation for an unforeseen event such as illness, natural disasters, loss of job, and an increase in tuition fee is not strange anymore. However, the way to respond it does not necessarily through the implementation of Islamic insurance. Adeney-Risakotta states that Indonesian have resources for facing risk in four different kinds of knowledge: mimetic, mythic, ethical, and theoretic. Islamic insurance represents the ethical and theoretic knowledge that provide introspection and moral responsibility, and rational understanding of risk.[475] However, this ethical and theoretic knowledge is still considered insufficient for many Indonesians. With this consideration, Islamic insurance in Indonesia is presented to the public with an emphasis on two aspects: religious validation and social features.

Many scholars indicate the Javanese ideals such as surrender to God will (*pasrah),* acceptance (*nrimo*), and gratitude are the reasons behind the lack of an insurance system within Indonesian society.[476] Islamic insurance is offered with a new theological narrative that

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[475] Bernard Adeney-Risakotta, "Is There a Meaning in Natural Disasters? Constructions of Culture, Religion and Science," *Exchange* 38, no. 3 (2009 2009), http://dx.doi.org/10.1163/157254309X449719.
[476] Cultural Psychology of Coping with Disasters: The Case of an Earthquake in ...
edited by Manfred Zaumseil, Silke Schwarz, Mechthild von Vacano, Gavin Brent Sullivan, Johana E. Prawitasari-Hadiyono. Safrina Thristiawati, Heath er Booth, Terence Hull, Iwu Dwisetyani Utomo. (2015) Self-rated Health of older persons in Indonesia. Asian Population Studies 11:1, page 44-66.

transcends people understanding of disaster, financial loss, and tragedy in general together with a practical solution to it.

The religious understanding of tragedies is a test from God, and it happens due to traditional disharmony in the society. Tragedies is something that we cannot control. It is in God's hand. The Modernist view transcend this by saying that there is a cause and effect for everything. Moreover, even if we cannot totally control what happens in the future, we can prepare for it. Indonesia as the land of seventeen thousand islands and volcanoes is well acquainted with tragedy. Through insurance tragedy is translated as a risk that can be mitigated and compensated. Islamic insurance goes further to convince Indonesian Muslims by stating that the Muslim can be risk-aware, more prepared but still God-minded. Islamic insurance ensures that risk is managed according to the laws revealed by God himself.

The discussion of lawful and unlawful is often to be too complicated for any lay Muslim to understand. Therefore, the way Islamic insurance is presented by the agent is that Islamic insurance is Islamic because the service necessitates the existence of Sharia board within the company. This Sharia board are a group of trustworthy Islamic scholars who monitor and ensure the service is following Islamic law.

Although Malaysia has a similar practice, the emphasis on religious scholars or institution rather than state support makes Islamic insurance in Indonesia is unique. The absence of trust towards the private company and direct support from the state make Islamic insurance companies rely on the religious institution or Muslim religious leaders. Riaz Hassan and Taghi Azadarmaki argue that in a differentiated social formation society in which religion and state occupy different space like Indonesia, people's trust toward religious institution tends to be higher than in un-differentiated social formation society.[477] The trust of Kyai or Islamic clerics in Indonesia is much higher compared to other Muslim countries.

Although this strategy has contributed to the growth of Islamic insurance in Indonesia recently, it is still considerably low. One reason is, as discussed previously, the increase in piety among Muslims in Indonesia does not necessarily mean support for a single expression of Islam.

[477] HASSAN, RIAZ, and TAGHI AZADARMAKI. "Institutional Configurations and Trust in Religious Institutions in Muslim Societies." *Islamic Studies* 42, no. 1 (2003): 97-106. http://www.jstor.org/stable/20837252.

Majority Muslims in Indonesia put the moral principles or Islam, such as justice and solidarity above a specific injunction found in the religious texts. The other reason is the impersonality of Islamic insurance as a formal institution. Islamic insurance claims to be a scheme that enables mutual help among the Muslims, unlike the for-profit conventional insurance. However, people tend to be willing to help and be charitable when they know the face of the person they want to help. This condition is particularly important for the constant repeated interaction and not one-off charity act.

Although many Muslim societies become more modern, they still withhold their communitarian way of socio-economic interaction. For instance, people in many Arab countries developed an informal model of interest-free financial arrangement. This arrangement between a homogenous group of people based on the principle of Mutual *Qard Hasan* (counter no interest loan), is well known as *Jamey'ah* (literally, Society). Each member pays an equal particular amount of money each month and the collected sum of money from the group is given each month to one of them.[478] In Kenya, almost 72 percent of the population participating in Saving and Credit Cooperative Societies (SACCOs) and have mobilized over Ksh.150 billion (USD 2.14 billion) in savings i.e. more than 30 percent of the National Domestic savings.[479] This type of informal arrangement is very popular especially with an estimated 72 percent of people living in Muslim-majority countries do not use formal financial services.[480]

In Indonesia, it is manifested in the tradition of *Arisan* or known as 'julu julu' or 'jula jula' in Sumatra. It is a form of informal rotating savings and credit association. Generally, this form of no-interest microfinance takes place during a social gathering at a fixed interval at each member’s home. This practice is still sustained nowadays representing a financial alternative to bank loans or other formal channels.[481]

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[478] Ahmed Al Ajlouni, "Personal Cooperatives Model: Basic Concepts and Evidence from Jordan.” *ISRA International Journal of Islamic Finance* 7, no. 2 (2015): 81-102,180.
[479] Kennedy Waweru, "An Investigation into the Cash Balance Management Approaches in Saving and Credit Cooperative Societies (SACCOs) in Nakuru County, Kenya."*Journal of Business Studies Quarterly* 2, no. 4 (2011): 17-26.
[480] Patrick Honohon, “Cross-Country Variations in Household Access to Financial Services.” Presented at the World Bank Conference on Access to Finance, Washington, D.C., 15 March 2007.
[481] Otto Hospes, ‘Women’s Differential Use of ROSCAs in Indonesia’ in Shirley Arderner and Sandra Burman (eds.): *Money-Go-Rounds: The Importance of Rotating Savings and Credit Associations for Women*, (Oxford: BERG, 1996): 127-148.

Beyond finance, the peasants in these traditional villages help others mutually in various activities from spontaneous help for mourning neighbors, collective maintenance of ancestral grave, agricultural activities, religious ceremonies, to building public facilities. Usually, they work together voluntarily since the beginning to the end of the activity without expecting material rewards for their work. This mutual aid is conducted based on different kind of reasons. Some societies implement this practice based on the principle of reciprocity. One will help someone else as long as he hopes he will get similar help from that person. Especially for major agricultural tasks in rice agriculture such as hoeing, plowing, planting, and harvesting, people will help others in order to get enough labor support when they need it.

These people also set up a rice barn collectively as a common food supply system. In rice-planting season, members of the group can use the rice or other staple foods (sagu, cassava, corn) for their need and repay it with equal amount when they harvest. Furthermore, this collective rice barn has two main functions; firstly, as emergency reserve during a famine and secondly as economic stability when there is oversupply and price of food goes down. Even for subsistence community such as *Baduy,* they do not sell their rice in the market but keep it in the rice barn called *Leuit* to provide community's daily need. Nevertheless, this mutual assistance in subsistence communities important not only in term of the economy (commodity stability) but also as part cultural identity.[482]

In this modern time, Indonesians try to implement this traditional way of mutual help in other matters too. *Arisan* for buying a car is one of the instances. Many of Indonesians are not wealthy enough to buy a car in cash. At the same time, they do not want to involve in a credit scheme because of the prohibition of usury. Therefore, they set up an informal saving group to help its member buying a car. This illustration shows that although Islamic insurance companies are successful in gaining trust from the public related to Sharia-compliant issues, Islamic insurance in Indonesia has not been successful in presenting the value of cooperation or risk sharing. In addition, one research in Medan, Sumatera island of Indonesia shows profit sharing

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[482] Francoise Gerard, Isabelle Marty & Erwidodo, "The 1998 Food Crisis: Temporary Blip or the End of Food Security?" In F. Gerard & F. Ruf (Eds.), *Agriculture in Crisis: People, Commodities, and Natural Resources in Indonesia, 1996 – 2000*, (Montpellier: CIRAD, 2001).

variable influences negatively and insignificantly on the local people's interest in Islamic insurance.[483]

The other strategy to boost public acceptance toward Islamic insurance, many Islamic insurance companies link their product with investment for social features. PT Sun Life Financial Indonesia promotes the waqf insurance benefits feature to attract customers. The feature that has been launched since August 2017. This service combines the concept of waqf (social endowment) and Islamic insurance that enables Muslims, in particular, to save continuously and at the same time assure their ability to establish an endowment. Customers who participate in such a plan will contribute to it regularly and, at the end of the policy, will bequest all benefit from it to appointed beneficiaries as a waqf endowment. The company works with Islamic NGOs to act as the trustee who allocates the funds collected to orphanages, religious schools, mosques, and other appointed beneficiaries. Syarikat Takaful Malaysia Berhad introduced a similar product in 2002. However, after 7 years of operation, the plan was canceled on 9 February 2009.[484]

The other social feature is micro Islamic insurance or known as microtakaful. Microtakaful is usually delivered by an Islamic insurance company in collaboration with domestic NGOs, which support Islamic microfinance institutions who offer microcredits and savings products. The NGO acts as an intermediary between the insurance company and the microfinance institutions which sell the credit-life microtakaful product together with their loans.

Takmin Working Group is a group of initiators who commit developing Islamic micro-insurance in Indonesia. Its members consist of experts in Islamic insurance, micro finance and accounting. Takmin Working Group (TWG) at first worked with PT. Syarikat Takaful Indonesia in developing and marketing the products. This approach, in the world's Microinsurance practice is known as the institutional approach or "Partner Agent Model". The Islamic micro-insurance serves the low-income clients and is utilized to help needy children or orphans to school, to cure the sick, to celebrate a family wedding, and to settle funeral of the death, etc.

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[483] Afrahul Fadilah Lubis, "Analisis Faktor-Faktor Yang Mempengaruhi Minat Masyarakat Dalam Memilih Asuransi Berbasis Syariah (Studi Kasus Pt Asuransi Takaful Umum Cab. Medan)" (University of Sumatera Utara, 2015), http://repository.usu.ac.id/handle/123456789/50419

[484] Rahman, Asmak Ab, and Wan Marhaini Wan Ahmad. "The Concept of "Waqf" and Its Application in an Islamic Insurance Product: The Malaysian Experience." *Arab Law Quarterly* 25, no. 2 (2011): 203-19. http://www.jstor.org/stable/23025247.

A robust civic tradition with distrust towards capitalism

This section discusses how the political repression and economic exclusion by the New Order regime toward Indonesian Muslims unwittingly generated popular Islam with a robust civic tradition, but a weak political and entrepreneurial institution. Although the recent democratization and economic liberalization have opened political space and increased people's welfare, there is still a high level of distrust towards state and market. This condition provides a path dependence that influences the development of Islamic insurance, which is presented as non-usurious but private-based insurance.

The development of the private sector in Indonesia, in general, came in fits and starts. The reason was that there was a long-standing distrust of private capital in Indonesia, particularly among the Muslim community.[485] Muslim population was considered as an important part of the country economic development and mobilizing them for achieving development goals through religious idioms had been vital for its success. President Soeharto, in his speeches, repeatedly regarded Islam and development as being inextricably interwoven. Soeharto argued these values should become the driving force and spirit of national development. Religion and development must equally support each other.[486]

Furthermore, Soeharto emphasized the critical role of the Islamic clerics (ulama) in revitalizing Islamic values as a positive spiritual and social force in national development. Soeharto urged the Islamic leaders to encourage the Muslim community to participate in the development and insisted that development is a religious duty. For this very reason, the government established the Council for Islamic Clerics (Majelis Ulama Indonesia, MUI) in 1975, in order to become a mediator between the government and the Muslim community as large.[487]

However, Soeharto's appeal to the Muslim population was an empty gesture. Not because, the lack of support from the Muslims, but because the priority of the New Order regime

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[485] Kian Wie Thee, *Indonesia's Economy since Independence* (Singapore: ISEAS-Institute of Southeast Asian Studies, 2012).
[486] Ali.
[487] Ibid.

was creating conglomeration within Indonesia economy and not helping the small and medium enterprises. Soeharto's rhetoric is merely a way to legitimize his economic agenda.[488]

In the late 1980s, discontent rose about the perceived widening gap between the privileged rich and the large group of poor people, specifically between the visibly wealthy ethnic Chinese business tycoons and the pribumi majority. The leading conglomerates, many of them ethnic Chinese tycoons had overgrown during the New Order. Their rapid growth was possible because of the patronage of the dominant political elite, particularly President Soeharto. Under this patronage, the conglomerates enjoyed preferential treatment, including substantial subsidized credits from the state banks, protection, and monopoly positions, and assured government procurement.[489]

Furthermore, the New Order government began to be criticized for not involving the native entrepreneurs (pribumi) in the development process and for allowing the special privilege to the Chinese minority. Muslim entrepreneurs were encouraged to study economics and business in the West so that they could compete with the Chinese in business. Criticism was leveled against the Government's marginalization of small-scale and middle-scale businesses in which many Muslims were involved. Soeharto's economic policies relied on the rapid growth of large private conglomerates which emerged and thrived under the patronage of Soeharto's 'New Order' regime. The too much emphasis on economic growth, rather than justice and dependence upon foreign aid rather than economic independence also became the target of critics. The criticisms came mostly from non-governmental organizations (NGO) with the support from international NGOs. Unlike in Malaysia under Mahathir Mohammad, the socio-political circumstances of the New Order had circumcised the development of Muslim entrepreneur class in Indonesia.

However, the absence of market economies among Indonesian Muslims and political democracy under the New Order did not obliterate the creation of civil institutions and public civility in Indonesia. On the contrary, the combination of economic exclusion and political repression forced Indonesian Muslims to occupy the civil society space, by focusing on

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[488] Thee.
[489] Ali.

proselytizing Islam to the society, establishing educational facilities, and setting up diverse NGOs and cooperatives which ironically mostly, if not all, owned by members of the economically weak groups.[490]

This emphasis on civil society rather than market or statist route is not new for Indonesian Muslims. Muslim Indonesia has historical precedence of creating public civility through the extra-state Muslim associations in late colonial Indonesia. Comparative research on politics and democratization in the 1980s and 1990s show that there are other ingredients besides market forces and democratic state that can make democracy work. Those two ingredients are 'social capital' and 'civil society'. Social capital consists of accumulative cultural endowments that facilitate the performance of specific social task. The common usage of civil society refers to the clubs, religious organizations, business groups, labor unions, human rights groups, and other associations located between the household and the state and organized on the basis of voluntarism and mutuality. According to Hefner, the practice of *pesantren* or traditional Islamic boarding school has civil precedence that provides a path of dependence for Indonesian Muslim society.[491]

Pesantren was a result of the destruction of imperial Islam and the loss of native rulers' authority during Colonialism. By doing that, the Dutch unwittingly reinvigorated popular Islam. The Dutch control of the state-led Muslim leaders in Indonesia to develop a cautious and critical attitude toward government and force them to rely on their own resources to build their institutions. Their situation contrasts with the experience of Muslims in much of the Middle East or even nearby Malaya (Malaysia). In Malaya, particularly in the native states subject to an indirect rule (where sultans retained a significant measure of authority), the British encouraged cooperation between state authorities and Muslim leaders. In Indonesia, little collaboration existed between colonial rulers and Muslims. In modern Indonesia, Pesantren has provided the leadership, organizational precedence for the birth of Civil Islam in Indonesia.

Pesantren also has a strong affinity with Sufism. In his study on the role of the Sufi organization, Salvatore argues that

[490] Hefner.
[491] Ibid.

> Sufi brotherhoods were at the forefront of a proto-globalization based on hemisphere-wide networking between metropolitan regions, rural provinces, and nomadic formations. Furthermore, cities became nodes within wider circulations, rather than, as in European and Weberian models, centers of corporate powers. The emerging patterns of civility were open-ended, balancing inner cultivation, communicative skills, and outward etiquette.[492]

Altogether, Hefner argues that Indonesia, in part due to deep pluralist traditions that predate colonial intervention and in part due to the role of civic associations in its recent democratic transformation, is a paradigmatic example of an 'emergent tradition' of civil Islam. According to Hefner, civil Islam is characterized by 'denying the wisdom of a monolithic "Islamic" state and instead affirming democracy, voluntarism, and a balance of countervailing powers in a state and society. According to Hefner, civil Islam of Indonesia confirms the commensurability of contemporary Islam and civil democratic traditions.[493] However, the case of Indonesia also shows the civil Islam of Indonesia has distrust towards the norms of modern capitalism.

A study compares several countries to understand what people really think about capitalism. The surveys conducted in early September 2015 by asking ten questions of population in ten nations Britain, the United States of America and Germany (from the developed world) and Brazil, India, Indonesia and Thailand from the faster growing, emerging world.[494]

The results show a high level of distrust towards capitalism among Indonesians. Only 3% of the respondents see the commensurability of business and the well-being of society. Almost half of the Indonesian respondents vie negatively toward the business practice of the company.[495] On the other hand, there is a high percentage of Indonesians who put the strong community and family life as important to well-being as a strong economy. In addition, while more people in all seven nations believe that the free enterprise system is better at lifting people out of poverty than government, in Indonesia only 8% confirms this belief.[496]

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[492] Armando Salvatore (2018) Sufi articulations of civility, globality, and sovereignty, Journal of Religious and Political Practice, 4:2, 156-174, DOI: 10.1080/20566093.2018.1439808
[493] Hefner.
[494] YouGov for Legatum Institute's Prosperity for All report as quoted by Jose Santiago, "What Do People Really Think About Capitalism?," (11 November 2015), accessed 2 November 2018, https://www.weforum.org/agenda/2015/11/what-do-people-really-think-about-capitalism/.
[495] Ibid.
[496] Ibid.

These surveys provide us with the social circumstances in which Islamic insurance has been introduced and developed in Indonesia. The initial development of Islamic insurance and Islamic economy in Indonesia came from this path. It did not come from a new middle class who began to embrace liberalism's privatization, or introduced by conservative Islam's bully state from above, but come as a critical voice against the market excess and political repression. Islamic insurance was a cultural expression of the identity of Indonesian Muslims. However, as the state had started to regulate it in the 1990s and market had become dominant in the process and uprooted from the civil society, Islamic insurance has lost its appeal for many Indonesian Muslims.

Also, the emphasis of Islamic insurance in the Sharia-compliant and not on the overall benefit of the products has only convinced the small number of Indonesian populations. As mentioned previously, with 91% of its population identify as Muslims, only 22% of the overall population (including the non-Muslims) perceive the laws in the country should strictly following the teaching of the Quran. In comparison, with 64% Muslim, there is 52% of the Malaysia population who has that view. The survey does not especially address Islamic insurance, and many of the proponents of Islamic insurance does not support the implementation of Sharia as a national law.[497] However, their argument is different from Civil Islam, which the supporters of Islamic economy mostly see religion as an individual matter. However, this survey still says something how the practice of Sharia-based institutions and products in society.

However, it does not mean that Islamic insurance is rejected by all Indonesian population. Rudnyckyj identifies a similar group as the New Malay entrepreneurs of Malaysia within many corporate settings.[498] Movements for spiritual reform active in state-owned enterprises, private corporations, and government bureaucracies in contemporary Indonesia represent a different phenomenon that Rudnyckyj describes as Market Islam. These groups are not necessarily interested in achieving broad social transformation through party politics or direct advocacy. They are not concerned with questions of human rights, social justice, or political liberalism:

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[497] Adeney-Risakotta.

[498] Rudnyckyj, Daromir. "Market Islam in Indonesia." *The Journal of the Royal Anthropological Institute* 15 (2009): S183-201. http://www.jstor.org/stable/20527696.

those who represent Islam as holding the key to economic success are, in general, not outspoken advocates for democracy.

Further, market Islam involves designing a form of Muslim practice commensurate with the goals of eliminating corruption, promoting privatization, and enhancing productivity in an increasingly global market. These groups are dominance within Malaysian society, but in Indonesia, they are a relatively small number. Market Islam is the group that is most likely to support the implementation of Islamic insurance in Indonesia.

Pepinsky further elaborates the characters of so-called Market Islam in Indonesia who is more likely to support Islamic financial institutions. He examines the socioeconomic origins of consumer demand for Islamic where expressed piety is on the rise. He discovers that piety is far less important as a factor in shaping individuals' use of Islamic financial products than commonly believed. The results show that the most pious Indonesian Muslims are just as likely to report using banking products as their less pious counterparts. However, Indonesian Muslims who have a high level of income and strong ties with other Muslim countries tend to use Islamic financial product. In other words, modernization and globalization play decisive roles in shaping individual use of Islamic financial products. Pepinsky argues:

> Islamic finance is a uniquely powerful symbol of identity politics in the Muslim world precisely because it is so nearly indistinguishable from conventional finance. The choice of Islamic financial products—at least in plural banking systems such as those found in Indonesia—is, therefore, a window into the ways in which social and economic changes are filtered through religion.[499]

Conclusion: distributional politics and critical Muslims in Indonesia

The first Islamic insurance of Indonesia was founded in 1994, or ten years after the establishment of Islamic insurance of Malaysia. This fact has been causing another delay for expansion and consolidation of Islamic insurance in Indonesia. This delay was not without reason: at a time when the Soeharto regime was consolidating the liberal economy through a centralistic approach, such an idea integrating an experiment into a national plan was not a popular path in

[499] Pepinsky, T. B. Development, Social Change, and Islamic Finance in Contemporary Indonesia, World Development (2012), http://dx.doi.org/10.1016/j.worlddev.2012.06.007

developmental planning. Moreover, a negative stigma to the initiative that carries Islamic agenda as a result of unpopular political Islam in the past is worsening any attempt to bring this case legitimate. Hence, when it first came into the ground as a micro-level experiment, it is out of the initiative of a small group of Islamic economic enthusiast influenced by the global spread that was aware with the limited opportunity available for pushing for a bigger agenda of a meso-level institution. Therefore, this early stage development was uniquely bottom-up pushed within a possible opportunity and rather an unconducive environment of the early New Order regime.

The changing environment of the New Order in the 1990s and afterward has provided a favorable circumstance for Islamic interest to advance their politics as in social and cultural affairs, but it must be emphasized that this does not mean the advance of a single, coherent ideology called 'Islam'. In Malaysia, the cooptation of ABIM by Mahathir Mohamad created a supportive condition for the Islamic modernist agenda including the development of private-based Islamic insurance. The state-led Islamization in Malaysia ensured that the development of Islamic insurance is compatible with the economic liberalization agenda and the ethnic politics of Malaysia. On the contrary, in Indonesia this agenda is only supported by the Modernist group of Indonesian Muslims.

The practice of Islamic insurance and Islamic economy was not agreed by all Indonesian Muslims. Although there has been less opposition since its establishment in the 1990s, the majority of Muslims in Indonesia see it as just one among many alternatives of the implementation of the doctrine of the Islamic economy. The modernists mostly promoted it as an expression of revivalism of Islamic identity, which encompasses not only in ritual but also in all aspects of human lives. However, the traditionalists reject the strict interpretation and stiff political position of the Modernists. The Traditionalists can be very strict on ritual rulings of the religion, but they are often to be more flexible in their socio-political position. In the issue of Islamic economy, the Traditionalists tend to emphasize on public benefit and avoid any radical confrontation with state authority compared to the strict adherence on particular interpretation on Islamic economic doctrine of the Modernists. Therefore, the Traditionalists are more susceptible to the state-sponsored social insurance of JKN-BPJS than private-based of Islamic insurance of Takaful. The JKN-BPJS is considered by the Traditionalists to be more consistent with

Islamic and Indonesian socio-economic values than the practice of contemporary Islamic insurance. The forum *bahtsul masail* pre-33th NU Congress held by PBNU at the Krapyak Yogyakarta boarding school on March 28, 2015, agreed to support the national health insurance program (JKN) which was handled by BPJS Kesehatan. They concluded that the JKN concept handled by BPJS Kesehatan was not problematic according to Islamic sharia. The forum which was attended by Muslim clerics from various regions in Indonesia determined that the BPJS was in accordance with Islamic law. They looked at the contract used by *BPJS Kesehatan* as ta'awun contract. When asked the question whether it contained usury, they answered that the BPJS contract did not contain usury.[500]

Furthermore, the emphasis on social benefit has been the primary goal of Islamic economy for many activist-minded of the pioneer of Islamic economy in Indonesia. As the political environment changed in the 1990s, more actors became more involved in the development of Islamic insurance. Conventional economists, bankers, actuaries and also lawmakers have become the primary actors of the recent development of Islamic insurance. Many pioneers feel that the idea of Islamic economy has been 'hijacked' by private sectors who emphasis more on finance. According to the pioneers such as Dawam Raharjo, moral concerns such as addressing poverty, inequality, and economic injustice, must be the main parameter of the success of any Islamic financial institutions. At this moment, he argues that many of these institutions merely focus on the increase in business indicators.[501]

Therefore, many Muslims in Indonesia are reluctant to support the Islamic economy and buy Islamic insurance premium. For many Indonesian Muslims Islamic model should be an alternative for capitalism and foreign domination and inculcated the spirit of self-help, solidarity, and cooperation. Recently, some Islamic insurance companies have been developing insurance-linked products, which combine financial protection with socio-religious investment. Other companies work with Islamic NGOs to deliver micro-takaful or micro Islamic insurance to the poor. However, it is very early to evaluate their impact on overall Islamic insurance development.

[500] Hafiz, "Pbnu: Akad Bpjs Sudah Sesuai Syariat Islam," NU Online, last modified 30 July, accessed 2 December, 2018. http://www.nu.or.id/post/read/61184/pbnu-akad-bpjs-sudah-sesuai-syariat-islam.
[501] Rahardjo.

The abangan or the nominal Muslims and the Non-Muslims see the current practice of Islamic insurance is quite exclusive. PDIP had been the strong opposition of Sharia-inspired regulations in the post-Soeharto era. Islamic finance had been seen as a symbol for Sharia encroachment to the multi-cultural and multi-religious Indonesia. As the Islamization of Indonesia become deeper recently and many santri, both Traditionalist and Modernist, have joined and become the constituents of PDIP there is less opposition from this party toward Islamic economy. PDIP has never opposed the idea of Islamic economy because it has become an acceptable practice in the society, but PDIP has been very critical in the implementation procedure of Islamic economy, particularly in the direct involvement of the state. According to PDIP, the Indonesian state should be neutral on this issue. The ideal Indonesian state should act only as a regulator of the Islamic economy, and not an incubator or supporter like the Islamist State of Malaysia. Moreover, any implementation of Sharia-based regulation must be in accordance with the national laws.

The lack of support of the state differentiates Indonesia's Islamic insurance with Malaysia's. The success of any Islamization agenda owes much to the involvement of the state. However, the problem for Indonesia lies in the ambiguity of the role of religion within a secular state. Especially Islam historically was considered to be a threat for the national and secular identity of Indonesia. Therefore, mobilizing support for Islamic finance or Islamic insurance had never been in the mind of the Indonesian government. Indonesia government allow the development of Islamic insurance to co-opt Muslims political aspiration but never fully support it in order to become the dominant part of the Indonesia economy.

Furthermore, the current government of Indonesia has been focusing more on building universal insurance coverage for its people. In order to do that, Indonesia needs to create a bigger risk pool. Indonesian citizen is under obligation to subscribe to the JKN, the national social security system. The wealthier population can add with private insurance if they need more coverage in their plan. In the context of contemporary Indonesia, private insurance is no substitute for the social insurance, but it is a complementary. Without this obligation, it can have detrimental effects on the risk pool. The government does not forbid Islamic insurance, but it does not encourage it either.

In sum, there is no full support from all political spectrums over Islamic insurance development in Indonesia. There are favorable circumstances for Islamic interest to advance their politics as in social and cultural affairs. However, it does not mean the advance of a single, coherent ideology called 'Islam', including 'Islamic economy'. There is only accommodation for the current practice of Islamic insurance within a wide variety of interpretations of Islamic doctrine and practices of social protection. In particular, the current manifestation of Islamic insurance has not enough support from the Muslim traditionalists.

Accordingly, the central question at the heart of the debate over Islamic finance in multicultural Indonesia, given that Islamic finance is nearly indistinguishable from conventional banking, is not one over the substance of the financial services provided by Islamic institutions rather. The question is about the extent to which the growth of an Islamic financial system in Indonesia is either costly or beneficial to Indonesians, Muslims and non-Muslims alike. In other words, the debate over Islamic finance is neither theological nor technical, it is distributional and political. The question is on how the Indonesian state should accommodate the demands of its citizens for financial products deemed to comply with Islamic principles.

In addition, Indonesia has failed to develop a fully-fledged regulatory state. Unlike Malaysia, the capacity of the Indonesian state to supervise and regulate the economy in accordance with market principle remains weak with a widespread corruption practice. This condition gives impact not only the development of Islamic insurance, but also the overall economic development.[502]

The social reason for the slow development of private-based Islamic insurance is the long-standing distrust of private capital in Indonesia. The amalgamation of rich precedents of the communal economy, economic exclusion, and foreign domination, and state repression by the New Order regime generate Islamic reform movement that emphasizes civil institutions and communal economic ethics. Rather than creating vibrant Muslim entrepreneurs but with conservative mindset like in Malaysia, the Civil Islam of Indonesia, as Robert Hefner define it, repudiated the goal of the Islamic state, mobilized religiously ecumenical support, promoted

[502] Rosser, in *Oxford Handbook on Asian Business System*.

women's rights, championed democratic ideals, and advocate an indigenous and egalitarian economy.

The initial development of Islamic insurance and Islamic economy in Indonesia came from this path. It did not come from a new middle class who began to embrace liberalism's privatization or introduced by conservative Islam's bully state from above but come as a critical voice against the market excess and political repression. Islamic insurance was a cultural expression of the identity of Indonesian Muslims. However, as the state had started to regulate it in the 1990s and market had become dominant in the process and uprooted from the civil society, Islamic insurance has lost its appeal for many Indonesian Muslims.

CHAPTER V

PAKISTAN

Pakistan is an ideological country. This country got independence from the British intending to provide a homeland for Muslims where they could live according to their religion. However, the goal had never been fulfilled as no government after independence paid serious attention to the Islamization of Pakistan. Although the constitution states Islam as the state religion, Pakistan retained the most law that inherited from the British and maintained the secularist traditions within the government. The concerted program of Islamization only started to take shape in 1977 when the left-wing government of the Pakistan People's Party (PPP) under Prime Minister Zulfikar Ali Bhutto was ousted in a coup d'état led by a former Army general, Zia-ul-Haq. He then became the sixth President of Pakistan with two cornerstones economic policy, including liberalization and Islamization of the economy.

The new government of Zia-ul-Haq showed some interest and announced many steps for Islamization. Establishment of the system of *Zakat* and Islamization of the banking system are important steps that need to be mentioned. A mandatory religiously derived tax called Zakat was enforced in 1980, which applied to saving accounts and other investment and to agricultural produce. In January 1980, the Pakistani government opened approximately 7,000 interest-free counters at all the nationalized commercial banks. Pakistan becomes the first country in the world with the highest number of Islamic banking.[503] Nevertheless, not enough attention was given to the insurance sector during that time.

In 1992, the Council of Islamic Ideology (CII) of Pakistan on its own initiative reviewed the insurance laws and proposed some changes. The council prepared a report "Islamization of Insurance" for the government in 1992, but the government did not consider implementing it practically. After a decade, the Securities and Exchange Commission of Pakistan (SECP), through notification S.R.O 877(I)/2012 dated July 16, 2012, issued Islamic insurance regulation of Takaful

[503] Aurangzeb Mehmood, "Islamisation of Economy in Pakistan: Past, Present and Future," *Islamic Studies* 41, no. 4 (2002).

rules, 2012, allowing conventional insurers to operate Islamic insurance windows alongside their existing conventional insurance business, and conduct Islamic insurance business. There were five Islamic insurance companies operated in 2015 with gross premium of US$ 64.34 million and an asset volume of US$ 114.38 million. The Islamic insurance industry comprised just about 2% of the insurance sector in Pakistan as at December 2015.[504] This number was still quite small compared to Malaysia and Indonesia within the same year.

This chapter examines the reason behind this existing gap between Pakistan and the two other countries: Indonesia and Malaysia in their Islamic insurance development. Moreover, it explains the reason why Pakistan delayed the development of Islamic insurance until 2012. In the early phase of its Islamization, Pakistan had preferred to focus on the implementation of Zakat in order to provide economic security for most of its poor population. This chapter begins with a brief section on the structure of Pakistan as an Islamic state. It elaborates its multinational characteristics, the status of Islam as the popular identity of the Pakistanis, the persistence of the kinship-based economic systems in the country, and the political actors related to Islamic insurance. This section focuses on the challenges that Pakistan has had in achieving a coherent national identity and becoming a stable nation.

The next section provides detail information on the growth and institutional development of Islamic insurance within the existing structure of the insurance sector in Pakistan. This section also discusses the linkage between Islamic insurance regulatory frameworks within the broader context of insurance or social protection in Pakistan. The state of Pakistan had always been idealized and positioned as the primary provider of the protection within the idea of the Islamic welfare state, and not merely as an incubator of Islamic insurance as Malaysia does, or as a regulator as Indonesia does.

The last two sections explain the factors for Pakistan's slow development of Islamic insurance through the lenses of 'political life' and 'social life' of Islamic insurance. The political life of Islamic insurance section explores the catalysts, the dynamics, and the political coalitions

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[504] SBP- 2015. Financial statements of financial sector. www.sbp.gov.pk quoted by Muhammad Hanif and Abdullah Iqbal, "An Evaluation of Takaful Insurance: Case of Pakistan," *Journal of Islamic Economics, Banking and Finance* 13, no. 1 (2014), http://dx.doi.org/https://doi.org/10.2139/ssrn.2386497.

behind the institutionalization of Islamic insurance, particularly during Zia's state-sponsored Islamization (1977-1988), and his continuous legacy in the aftermath. The central puzzle to be addressed is why, as an Islamic state, Pakistan has been slow or even failing in creating Islamic reform for its insurance sector. Next, the social life of Islamic insurance section explores the process of how Islamic insurance was introduced by the Islamist modernizers within a highly conservative social-cultural environment of Pakistani society. Similarly, it asks the question of how Islamic insurance has not been receiving proper acceptance by a society where Islam is deeply ingrained in its norms, values, and identity.

The structure of a 'weak' Islamic state

The Islamic Republic of Pakistan had been created in the name of Islam. Muhammad Iqbal (1876–1938), a poet and philosopher who is called the 'Spiritual Father of Pakistan' pioneered the idea for a separate land for the Muslim of India in his famous 1930 Allahabad Address. Iqbal described Islam as a "social *nizam*" (social order) and argued that the religion of Islam was the best suited of all religions for the organization of life, as it applied to every aspect of the life of the individual and society.[505] Furthermore, although few argued that Muhammad Ali Jinnah, the founding father had preferred a more secular type of Pakistan, it is commonly believed that the Muslim League leadership including Jinnah and the *ulama* (Islamic clergy) had articulated their vision of Pakistan in terms of an Islamic state as Iqbal previously described.

The Constitution was adopted on 23 March 1956, and from then on, Pakistan is known as the world's first Islamic republic. However, the role of Islam in the Republic was not clearly defined. In 1973, the new constitution was promulgated, in which Islam is stated as the state religion. The 1973 Constitution provides the framework that no law would be passed against the teaching of Quran and the Sunnah (Prophetic tradition). However, Islam was never enough to make Pakistan into a unified nation; Pakistanis are divided not only by different variations of Islam but also by a host of other ethnic, linguistic, cultural, and social difference.

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[505] Emmy Abdul Alim, *Global Leaders in Islamic Finance Industry Milestones and Reflections* (Singapore Hoboken, New Jersey : Wiley, 2014).

A multinational country

Pakistan is the world's sixth-most populous country in the world and has the largest Muslim population after Indonesia.[506] Like Indonesia and Malaysia, Pakistan is also a culturally diverse country. In term of geographical area, it is the 36th-largest country, spanning 881,889 square kilometers (340,499 square miles). Pakistan has a 1,046-kilometre (650-mile) coastline along the Arabian Sea and the Gulf of Oman in the south and is bordered by India to the east, Afghanistan to the west, Iran to the southwest, and China in the far northeast.[507]

Pakistan is a federal parliamentary republic. Executive power is headed by the prime minister, who works coherently along with the bicameral parliament and the judicature. President is the head of the state. Like the presidential election system in the US, president is elected by the Electoral College for a five-year term. The president was the most important authority in the country until 2010. The 18th amendment, passed in 2010, stripped the presidency of its major powers.[508] Before the amendment, the president had the ability to remove the prime minister and dissolve the Parliament. The amendment turned Pakistan from a semi-presidential to a parliamentary republic.

The name Pakistan means *Land of (the) Spiritually Pure* in both Urdu and Persian languages. In 1933 Choudhary Rahmat Ali, a Pakistan Movement activist, proposed 'Pakstan' as the name of the country in his paper *Now or Never; Are We to Live or Perish Forever?* This paper is also known as the "Pakistan Declaration". The name of Pakistan is an acronym that stands for the "thirty million Muslim brethren who lived in PAKSTAN—by which we mean the Five Northern units of India: Punjab, Afghan Province, Kashmir, Sind, and Baluchistan". The letter i was added to ease pronunciation and forms the linguistically correct and meaningful name. [509]

Another prominent leader for Pakistan movement was the poet-philosopher, Muhammad Iqbal. Iqbal who was born on Nov 9, 1877, encouraged the creation of a "state in

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[506] Pew Research Center, *Interactive Data Table: World Muslim Population by Country*, November 17, 2017 ed. (2017).
[507] Lawrence Ziring and Shahid Javed Burki, *Pakistan*, April 12, 2019 ed. (Encyclopædia Britannica, inc., 2019).
[508] National Assembly of Pakistan, *Report of the Constitution (Eighteenth Amendment) Act*, by National Assembly of Pakistan (2010).
[509] Choudhary Rahmat Ali, *Complete Works of Rahmat Ali* (Islamabad: National Commission on Historical and Cultural Research, 1978).

north-western India for Muslims" in his 1930 India Muslim League presidential address at Allahabad, British India. As a leading philosophical and literary voice during the time of Indian independence and the eventual partition of the country, Iqbal was an essential political and social leader in the establishment of Pakistan in 1947. Although he died in 1938, which is long before the establishment of independence Pakistan, he gave vision to the people particularly to Muhammad Ali Jinnah, *Quaid-i-Azam* (the Great Leader) and *Baba-i-Qaum* (Father of the Nation) of Pakistan, through his poetic collections.[510]

Following Iqbal's vision, Jinnah tried to build a strong state relying on three principles of 'one nation, one culture, and one language'. He also believed that Pakistan could somehow be turned into not only an ideal Islamic state but also an ideal egalitarian socialist state. Jinnah aspired the very solid traditions of social justice in Islamic thought could somehow be made to flourish in an independent Pakistani state.[511] However, many scholars argue that these visions neglected the social and geographical base of Pakistan. In reality, Pakistan has never been able to reach a consensual conception of the nation since its independence. The ideological foundation for Pakistani state nationalism led to the partition of India has failed to act as a unifying concept for the multinational country of Pakistan. [512]

The land of Pakistan was part of British India. As a state, Pakistan was born out of India's partition in 1947. The initial rationale for separating Pakistan from India was the presumed need to provide a homeland for the minority Muslims in an overwhelmingly Hindu India. It was a result of the two-nation theory stating that Muslims and Hindus are two separate nations by every definition; therefore, Muslims should be able to have their separate homeland in the Muslim majority areas of India, in which Islam can be practiced as the dominant religion.

In 1946, the Labor government in Britain decided to end the British rule of the Indian Subcontinent. The loss of international support on continuing India colonialization, numerous local protests, and financial burden of World War II forced the British to take this decision. The Indian National Congress demanded a single state, while the Muslim League, which made up

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[510] Alim. Page 4.
[511] Anatol Lieven, *Pakistan a Hard Country*, 1st ed.. (New York: New York : PublicAffairs, 2011).
[512] Christophe Jaffrelot, *Pakistan Nationalism without a Nation?* (New Delhi : New York: New Delhi : Manohar : Centre de Sciences Humaines, 2002).

most of the Pakistani elite after 1947, expressed the idea of a separate Pakistan as an alternative. The British proposed a compromise in the form of a decentralized state with much power given to local governments. However, this proposal was rejected by both of the parties and resulted in several riots in South Asia.

Eventually, the Parliament of the United Kingdom agreed to divide British India into the two new independent dominions; the Dominion of India (later to become the Republic of India) and the Dominion of Pakistan (later to become the Islamic Republic of Pakistan).[513] Fifteen million people were displaced due to religious violence accompanied the partition across the subcontinent. On 14 August 1947, the new Dominion of Pakistan became independent, and Muhammad Ali Jinnah was sworn in as its first governor-general in Karachi.[514]The tragic experience of partition became the basis of a strong India-centric threat perception in Pakistan.

At the time of its independence in 1956, Pakistan had two separate geographical entities. The eastern part is only one-sixth the size of the western part of Pakistan yet holding eight million more people. The western part of the country possessed 80 percent of the cultivable land and had the country's capital and only port in Karachi. Meanwhile, East Pakistan had far less infrastructure and was much weaker economically.

Both parts of Pakistan were mainly Muslim. However, there were differences in religious practice. The Muslims in the western part of Pakistan has a long history of communal strife, which influences the relationship between different religious communities in the area. On the contrary, religious interaction with Hindus had become routine for Bengalis in the east. According to Weightman, those cultural differences were some of the centrifugal forces that would ultimately result in its political demise leading to the transformation of East Pakistan into Bangladesh in 1971.[515]

The split indeed created an Islamic trend within the country, but it did not necessarily create a cohesive nation of Pakistan. It is mainly due to the lack of linguistic cohesion among

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[513] *Indian Independence Act*, by UK Parliament (1947).
[514] William Dalrymple, "The Great Divide: The Violent Legacy of Indian Partition," *the New Yorker*, June 22, 2015, 2015, accessed November 4, 2018, https://www.newyorker.com/magazine/2015/06/29/the-great-divide-books-dalrymple.
[515] Barbara A. Weightman, *Dragons and Tigers: A Geography of South, East, and Southeast Asia* (Taylor & Francis Ltd., 2002).

Pakistanis. About two-thirds of the population speaks Punjabi. Punjab is the most economically productive province and contains the modern nation's capital, Islamabad. Sindhi language is spoken by about 12 percent, mostly in Pakistan's second industrial province of Sind. Urdu is spoken by only 8 percent, yet it was proclaimed the national language. Urdu is also the language of the state education system, of the national newspapers, and the film industry. It was the language of Muslims in the heartland of the old Mughal Empire, centered on cities of Delhi, Agra, Lucknow, Bhopal, and Hyderabad, rooted in what is now India.[516] Along with English, Urdu is the language of the elite and government.

The acknowledgment of Urdu as the official language of the country does not correspond with the social practice by majority Pakistanis. Urdu-speakers are concentrated in cities, especially the old capital of Karachi. Those are the Mohajirs, people who migrated from India after partition in 1947. Several other languages are spoken, with the most enormous diversity in mountainous regions. Pashto and Baluchi belong to the Iranian branch of the Indo-European language family. Sindhi, Urdu, and Punjabi belong to the Indic branch. Brahui is a Dravidian language of about 2.2 million people with the vast majority found in Baluchistan. There is also Balti, which is a Sino-Tibetan language used by people living in Gilgit-Baltistan region of Pakistan.[517]

Nonetheless, Pakistan has a geographical unity that in some respects thousand years old, being the valley of the River Indus, which drains southward into the Arabian Sea plus neighboring mountains, deserts, and swamps. This Indus plain was the ancient site of one of the oldest civilizations of Mohenjo-Daro. After the coming of Islam, people in this geographical entity had been professed the religion Islam for hundreds of years and have often been ruled by the same Muslim dynasties.[518] However, the geographical characteristics of having high altitudes and desserts have also limited the accessibility and people interaction, which foster cultural differentiation, communalism, and regionalism within the country.

Pakistan is politically divided into four highly differentiated and unequal parts: Northwest Frontier Province (NWFP), Punjab, Sind, and Baluchistan. Waziristan is not a province but is part

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[516] Ibid.
[517] Ibid., page 180-182.
[518] Anatol Lieven, *Pakistan a Hard Country*, 1st ed.. ed. (New York: New York : PublicAffairs, 2011), page 11.

of the Federally Administered Tribal Areas (FATA).[519] NWFP is capped by a dramatic knot where the Karakoram, Pamir, and the Hindu Kush have buckled together. Peshawar is the biggest city and industrial center of this region. Most people living in this area are Pathan and speak Pashto. Waziristan is also a mountainous region, but it is bordering with Afghanistan. The majority of followed the customary law of Pashtunwali, and only small number of them following the State law. Badal-revenging blood feuds to protect *Zan* (family), *Zar* (wealth), and *Zameen* (land) are central pillars of this code.[520]

The Punjab region long had been the breadbasket of the subcontinent. Moreover, Punjab, on average, produced more than half of the GNP of Pakistan. Punjabi has continuously also dominated the armed forces. Sind region is located in the Indus delta, which make it very fertile for agriculture. Second to Punjab in size and wealth, Sind has excellent agricultural potential and in 1947 was in the process of being colonized by immigrants from Punjab. However, much of the rural Sind remains controlled by *zamindari*. Initially, zamindari collected taxes for the Moghuls and later the Raj. Zamindar were or became large landowners, especially in Sind and Punjab, and they continue to control both land and peasant farmers under the feudal system. Politically, Zamindari families are often voted in as members of Pakistan's Parliament because they are relatively wealthy and come from prominent families. Baluchistan has twice the size of Punjab, but it is rugged and arid. Baluchistan possesses the smallest population and is the most impoverished province.[521]

This diversity has created various localized ethnic identities and loyalties, arguing for cultural recognition in a more inclusive national narrative, struggling for political autonomy, or more significant share of the economic development. For instance, Sindhi nationalism evolves in a rural setting of Sind under the leadership of prominent large landowner families, Baloch nationalism flourishes in a tribal milieu requesting the more significant share of the profits from mining and other industries, and the *Mohajir* movement in an urban context of Karachi.[522] Those

[519] Weightman.
[520] Ibid.
[521] Ibid., page 183-186.
[522] Farhan Hanif Siddiqi, *The Politics of Ethnicity in Pakistan: The Baloch, Sindhi and Mohajir Ethnic Movements* (Routledge, 2012). And also see Alyssa Ayres, *Speaking Like a State: Language and Nationalism in Pakistan* (Cambridge University Press, 2009).

localized loyalties are counter-reactions toward the increasing dominance of the Punjabi in Pakistan's bureaucracy, military, and industries.

Modern multinational Pakistan has been governed by following the legacy the British in ruling British India. Instead of direct control through a powerful centralized government, the British relied on local chieftains, landowners, or provincial leaders to manage the population. Similarly, the 'weak' federal government of Pakistan has always depended on the very same old elites and families in governing the country. The framework of a federal parliamentary republic and meritocracy are supposed to overcome political problems generated from those diversities. However, those modern institutions have not been able to transform Pakistani society.

Islam as the state and the popular identities

The Constitution of the Islamic Republic of Pakistan, also known as the 1973 Constitution, incorporates many injunctions from the Sharia. The 1973 Constitution is considered to be one of the most Sharia-dense constitutions in the modern world. Besides stating that Islam is the state religion, the 1973 Constitution uses language, norms, principles, prohibitions, and guarantees derived from Islamic law. [523]

Pakistan was the first country in the modern world to adopt the adjective "Islamic" to modify its republican status under its otherwise secular constitution in 1956. However, Islam has only become state religion after 1973, when a new constitution, more democratic and less secular, was adopted. The Constitution of 1973 is Pakistan's most important document as it gives foundation of the current government. Article 227 of the Constitution holds that all existing laws "shall be brought in conformity with the injunctions of Islam as laid down in the Holy Quran and Sunnah […] and no law shall be enacted which is repugnant to such injunctions." [524] Still, the very legal structure in Pakistan is common English law, which inherited from the former British ruler. With time, Pakistan introduces legal changes to accommodate new developments.

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[523]Corri Zoli and Emily Schneider, "How Islamic Is Pakistan's Constitution?," *Foreign Policy*, May 15, 2014. https://foreignpolicy.com/2014/05/15/how-islamic-is-pakistans-constitution/.
[524]Ibid.

Pakistan's legal system contains State law, Sharia law and Customary laws. State law and Sharia law are both formal, written codes. Meanwhile, customary laws are informal and unwritten, but immensely strong, because they reflect the cultures of the people.[525] In so-called Tribal Areas of the Northwest Frontier Province, the government in Pakistan relies on the local authority to maintain order. Instead of Pakistani state law, a body of local elders and notables or the leading males of families so-called the *Jirga* implement *Pashtunwali*, the ethnic code of the Pathans. The Pashtunwali provides a general guideline for resolving disputes once they arise. The traditional codes of Pakistan do not provide detail rules for every contingency. The normative content of customary laws is very fluid; therefore, it is best thought as a code of honor rather than a legal code. Instead of trying to abolish crime altogether, maintaining collective honor and prestige, restoring peace, and retribution are the primary purpose of this ethnic code. Also, this code influences how they conduct their economy. [526]

Beside the Pathans, every traditional Pakistani community has its version of customary laws. The only significant population in Pakistan which has completely shed allegiance to traditional codes are the *Mohajirs* (the migrants) of Karachi.[527] The Mohajirs of multi-ethnic origins migrated from various regions of India to Pakistan after the separation.

The Sharia is often considered to be more progressive than Pashtunwali. For instance, Sharia guarantees a share of inheritance to girls, while Pashtunwali gives it only to boys; furthermore, Sharia law guarantees rights to wives in the case of divorce. However, the Sharia that was promoted by the Taliban, both in Afghanistan and Pakistan, does not necessarily mean the Islamic law as understood and implemented in many other Muslim societies. The Sharia that is being advocated is the tribal interpretation of Sharia by the Taliban.[528] Despite its progressiveness, the implementation of Sharia is complicated in Pakistan, because the different Islamist groups in Pakistan cannot have consensus which form of the Sharia is valid.

According to Ian Talbot, one of the leading historians of South Asia, the separation of East Pakistan into an independent country of Bangladesh in 1971 contributed to the trend toward 'a

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[525] Akbar S. Ahmed, *Pukhtun Economy and Society Traditional Structure and Economic Development in a Tribal Society* (London: London, 1980).
[526] Lieven.
[527] Ibid.
[528] Lieven.

more Islamic' Pakistan in three ways. Firstly, it cut stroke the numerical strength of the non-Muslim minority. Secondly, it strengthened anti-Hindu and anti-Indian sentiment by seeing that the East Bengali secession was a conspiracy, and lastly, it demolished the secular Pakistani nationalist ideology, which had huge supports among the Bengalis. The secession of East Pakistan into a new country of Bangladesh reinforced Islam as an ideological cement for the state of Pakistan.[529]

After the secession, the Pakistan People's Party (PPP) under Bhutto (1973-1977) advocated a program compounded of agricultural and industrial reform and the promulgation of new constitution 1973, which defined Pakistan as an Islamic socialist republic. The president and prime minister were to be Muslims, and laws were to conform to Islam as determined by the council of *Ulama* (Islamic clergy). As Pakistan became increasingly dependent on oil-rich Arab states for loans, commerce, and employment of labor, Bhutto made further concessions to Islamic morality, such as prohibiting alcohol and gambling.[530] Furthermore, the regime of Zia-ul-Haq of the late seventies intensified this Islamization process by utilizing Islam as a tool for nation-building bypassing other traditional loyalties.

Islam is deeply ingrained in the identity of Pakistani people. Even the PPP, which is generally regarded as 'secular' party, has been using religious symbols to gain support from the population. The PPP recruited many of its politicians from the prominent families, specifically families of hereditary saints. However, Islam of Pakistani masses contains various traditions. Pakistan contains all the key facets contemporary Islam: Sufism; traditionalist scholars; the modern clergy and their madrasah and Islamic colleges; Islamic parties and their political activists; and Islamic modernism.[531] Therefore, there is always a strong reaction when certain groups or the state itself tries to impose one monolithic version of Islam imitating, for instance, Saudi Arabia, Sudan, or Iran.[532]On the other hand, the Pakistani state is too weak to achieve this even if it wanted too-as Zia-ul-Haq's failed Islamization demonstrated.

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[529] Ian Talbot, *Pakistan, a Modern History*, Expanded and updated ed.. (New York, NY: Palgrave Macmillan, 2005). page 32.
[530] Lapidus, 646
[531] Muhammad Qasim Zaman, *Islam in Pakistan: A History* (Princeton University Press, 2018).
[532] Lieven.

The majority of Muslim in Pakistan is Sunnis, and most of them are traditionalists known as *Barelvis.* The name comes after the madrasah founded in 1880 in the town of Bareilly-also in Uttar Pradesh, India. They have a traditional religious attitude, which are inspired by Sufism. This popular Islam includes a belief in the intercession of saints with God, the validity of miracles by the saints, worship at the shrines of saints (though not strictly speaking worship of the saints), and local traditions attached to the saints.[533] The practices of Barelvi may similar to the practice of the older Muslim societies; however, the traditionalist orientations had begun to take a recognizable shape only in the late nineteenth century as a response to modernism.[534]

Unlike the *Nahdlatul Ulama* in Indonesia, the Barelvis have never created a significant and enduring political party of their own. They played a leading part in all the broader Muslim mass movements in India and Pakistan, and then formed part of the MMA Islamist alliance which governed the NWFP and Balochistan from 2002 to 2008. However, their political influence is very limited.

Based on their theological understanding, all the Sunni Islamist groups, from the relatively moderate and democratic *Jamaat-e-Islami* to the *Taliban* and other extremists, are drawn from one of two traditions: the *Deobandi* and the *Ahl-e-Hadith*.[535] The *Deobandi*, named after a famous madrasah founded in Deoband (now in Uttar Pradesh, India) in 1866, is a representation of one of the oldest Islamic modernisms. Both Pakistan's main Islamist parties today, the Jamaat-e-Islami (JI) nationally and the Jamiat-e-Ulema-e-Islama (JUI) in the Pathan areas, are drawn from the Deobandi tradition.[536] Another tradition is so-called *Ahl-e-Hadith*. It is a branch of the international Salafi tradition, heavily influenced by Wahabism. The Ahl-e-Hadith are more extreme than the Deobandis, and less concerned with questions of modern social justice and development.[537]

The most central from all Islamist ideas is the idea that sovereignty belongs to God alone. The implication is that all legal and political authority derives from God and His injunctions, as

[533] Ibid.
[534] Zaman.
[535] Lieven.
[536] Ibid.
[537] Ibid.

mentioned in the Sharia. According to the Sunni Islamists, one could not be a Muslim without accepting this idea, nor could a state become Islamic without recognizing it.[538]

Beside this majority Sunnis, Pakistan also hosts so-called Muslim minorities. There are two 'Muslim minorities' in Pakistan: the Ahmadis and the Shias. Seven million or 2.2% of Pakistanis are Ahmadi. The Ahmadiyya follows the Sharia injunctions in their rituals and shares many ideas with the Islam modernists, except the Ahmadis believe that their leader, Mirza Ghulam Ahmad, was also a prophet after Muhammad. Because of this belief, Ahmadiyya was declared as a non-Muslim minority of Pakistan in 1974.[539]

The Shias of Pakistan are the world's second-largest Shia community after that of Iran. The Shia comprises only 10-15 percent of Pakistan's population (20-30 million). Although there are many incidents where Sunni extremists targeted the Shia group with hate propaganda and terrorism, Shias have always been fully integrated into all sections of political, professional, and social life without suffering any discrimination. In mainstream politics, the Shia-Sunni divide has never been an issue in Pakistan. Two prime ministers from Bhutto family, Zulfiqar Ali Bhutto and his daughter, Benazir Bhutto, were also Shia. Moreover, Shia clergy has been at the forefront of communal activism in Pakistan since 1949, but the general Shia people participated in such organizations, as they had in pre-partition India.[540]

Islamist radicalism in Pakistan is influenced by a combination of ideology and conditions induced by the governing elites. Similar to what happened during the partition of 1947, Muslim masses can occasionally be stirred up to furious panic by the cry of "Islam in danger'.[541] The governing elite and the military of Pakistan also often create conditions that foster Islamic radicalism. For instance, many of religiopolitical related violent incidents happened after Pakistan's realignment in the US-led War on Terror in the aftermath of September 11, 2001.[542]

All in all, traditional and popular forms of Islam do play a key role in holding Pakistan together. However, their role is not on the modern sense of transforming the sociopolitical conditions as the forces of Islamist reform (whether moderate or extremist) would wish. Islam

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538 Zaman.
539 Ibid.
540 Andreas Rieck, *The Shias of Pakistan: An Assertive and Beleaguered Minority* (Oxford University Press, 2015).
541 Lieven, page 127-128.
542 Ibid.

as a single homogenous ideology, is not present in the mind of the majority of Muslim Pakistanis.[543] Islam indeed provide elements in the nation-building process of a multinational Pakistan. The religion also has a significant role in transforming the moral of the society, like the case of Malaysia's corporate sector mentioned before where Islam is utilized to inculcate discipline and work ethics among the workers. Some Pakistani statesmen have tried to promote religion in public life as a way of trying to improve working ethics of public officials.[544] However, Islam in Pakistan has failed to create loyalties and ethics, which transcend those of loyalty to kin. This kinship loyalties and ethics are quite robust that influence in not only politics but also the economy of Pakistan.

'Patronage to kinship' economy

In term of economy, around a quarter of Pakistan's Gross Domestic Product (GDP) and its export earnings are derived from the agricultural sector, which is controlled by a few thousand feudal families. With this concentration of economic power, the feudal families also have considerable political power upon the country. In addition to agriculture, remittance is an important part of Pakistan's economy. Around 7 million Pakistani Diasporas contributed significantly to national economic stability. In 2015-2016, they transferred money to their families amounted US$19.9 billion of remittance or equaled to 7.11 % of Pakistan's GDP.[545] Ian Talbot argues that remittance was one of the contributing factors for Zia-ul-Haq longevity in power, rather than his hegemonic Islamic discourse.[546]

Modern industries are rare, and they are only available within the metropolitan areas of Karachi and Lahore. Most of the urban population remains semi-employed or informally employed. Pakistan was ahead of South Korea in economic development in the early 1960s, but now, it is dreadfully far behind. Nonetheless, with the continuous conflict in the neighboring country, Afghanistan, the constant threat of violence and terrorism, and the prevalent corruption

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[543] Ibid.
[544] Ibid., page 125.
[545] Shahid Iqbal, "$20 Billion Remittances Received in Fy16," *Dawn*, 16 July, 2016, accessed 20 February 2017, https://www.dawn.com/news/1271081.
[546] Talbot, *Pakistan, a Modern History*., page 245.

within a weak government, Pakistan is not a fail state. In fact, Pakistan is quite functional as a state and even can be considered as one of the most resilient countries in the world.

Pakistan's average economic growth rate in the first five decades (1947–1997) has been higher than the growth rate of the world economy during the same period. Also, Pakistan's manufactured exports in the 1960s were higher than those of Malaysia, Thailand, the Philippines or Indonesia. However, because of the lack of investment in education, training, skills, and health of the labor force, Pakistan is now behind those countries.[547]

The country is one of the largest producers of natural commodities. Pakistan's most important industry is textiles, and this industry has an overwhelming impact on the economy of the country. The textile sector in Pakistan represents about 57% percent of the country's exports.[548] This industry is the second-largest employment sector in Pakistan, with approximately 40% labor force in the industry. Pakistan also develops other industries, such as mining, oil and gas extraction, and automotive.

Although the agriculture sector still plays an important role, and the manufacturing starts to grow, the current economy of Pakistan is shifting toward services. The services sector share in GDP stands around 44.18 percent on average.[549] The share of the services sector in total employment has been increasing over time. In 2009, 2.76 million people were employed in this sector. However, the financial sector, which includes insurance, real estate, and business service has still a small share in employment generation, which employed only around 820,000 people.[550]

The Pakistani economy is also sustained by the remittance transferred by its diaspora. In 2015-16, there was US$19.9 billion remittances came from 7 million Pakistani diasporas. The primary source countries of remittances to Pakistan are the United States and the Gulf states.

Since the late 1980s, Pakistan has pursued a program of market-oriented economic adjustment, reform, and development with the support of the International Monetary Fund

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[547] Ishrat Husain, "The Economy of Pakistan: Past, Present and Future," in *Islamization and the Pakistani Economy*, ed. Robert M. Hathaway and Wilson Lee, Asia Program (Washington, D.C.: Woodrow Wilson International Center for Scholar, 2004), page 16.
[548] Textile Industry Division Government of Pakistan, "Textile Division," accessed April 24, 2019. http://www.textile.gov.pk/.
[549] theGlobalEconomy.com, *Pakistan: Share of Services* (2017).
[550] Ayas Ahmed and Henna Ahsan, *Contribution of Services Sector in the Economy of Pakistan* (Pakistan Institute of Development Economics, 2011), http://www.pide.org.pk/pdf/Working%20Paper/WorkingPaper-79.pdf. page 12.

(IMF) and bilateral donors. this program has aimed at enhancing macroeconomic stability, promoting the private sector and export-led industrial development, and reversing past neglect of critical social sectors such as health, education, and population planning. Unfortunately, the implementation of this program has mostly lagged expectations. The main reason was the liberalization program was absorbed by the Islamization of the economy.[551]

Pakistan has everything needed to be successful economically. Although there are plenty of cheap labor, a large domestic market, and access to regional markets, foreign investors have been reluctant to invest their money in Pakistan. Its widespread corruption, lack of skilled labor, law and order problems, and outdated infrastructure are some of the reasons behind that. Another major problem is Pakistan's massive external debt and its continued dependence on financial aid. Debt and foreign grants provide approximately 25 percent of government revenue, and debt service obligations total nearly 50 percent of government expenditure.[552]

Underlying most of the economic problems faced by Pakistan is the persistence of its 'patronage to kinship' system. Patronage has long been the bedrock of politics in Pakistan, where votes are dictated by immediate concerns about legal protection and government handouts.[553] It explains the mass support for populist ideas and programs such as 'Islamic welfare state' introduced by Pakistan leaderships, including the current Prime Minister, Imran Khan.

Pakistan is low in natural resources, such as oil and natural gas, there is no 'traditional' source of wealth for elites to control and monopolize, Lieven explained. In this environment, the only way to extract wealth is through control over the state. To achieve control over the state, communal leaders rely on "patronage to kinship" – an underlying dynamic of the Pakistani system where wealth and power are distributed along the kinship line. This deep kinship, Lieven noted, is a vital aspect of Pakistani society. Beside to gain wealth, kinship is used to maintain degrees of stability through power structures.[554] This character provides the basis for the whole explanation

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[551] Yasmeen Niaz Mohiuddin, *Islamization and Liberalization of the Economy under the Military Government of General Muhammad Zia-Ul-Haq: 1977-1988*, *Pakistan: A Global Studies Handbook* (Washington DC: ABC-CLIO Inc., 2007).
[552] *Nations Encyclopedia*, s.v. "Pakistan-Overview of Economy," accessed 7 April 2018, https://www.nationsencyclopedia.com/economies/Asia-and-the-Pacific/Pakistan-OVERVIEW-OF-ECONOMY.html.
[553] Lieven.
[554] Ibid.

of the stagnation of Islamic insurance in Pakistan, which will be elaborated further in the upcoming sections.

However, this endemic patronage does not necessarily make the economy of Pakistan a failure. On contrary, the strong kinship was one of the reasons for its resiliency. The economy proved to be resilient in the face of multiple adverse events concentrated into a four-year (1998–2002) period: the Asian financial crisis, economic sanctions, the global recession of 2001–2002, a severe drought, and refugee crisis in the post-9/11 military action in neighboring Afghanistan.

Political actors of Islamic politics

The following paragraphs provide a brief map of the actors of Islamic politics in Pakistan, particularly on their positions regarding the institutionalization of Islamic insurance. As mentioned before, patronage and kinship form the essential elements of the Pakistani political system. In Pakistan, political factions, which support individual politicians or alliances of politicians are significant, but they are temporary. Politicians use factions to seek patronage because they need the foundation of strong kinship networks, which are the most important aspect of Pakistani politics.[555]

Although there have been power shifts within the society, the landowners are still the dominant power in Pakistan's politics. A few thousand feudal families control Pakistan's agricultural sector. Only two percent of households have landholdings larger than 20 hectares, accounting for 30 percent of total land holdings.[556] Although successive military and civilian governments have tried with to redress the land imbalance, the concentration of economic power in Pakistan still rests on these families. As a result, feudal lords continue to wield more power than civil authorities do in many rural areas. This concentration of economic power strengthens these individuals' influence within the patronage and kinship patterns of the Pakistani political system.

However, great individual landowners no longer dominate the southern part of Punjab and the NWFP. Several land reform program, the subdivision through inheritance of formerly

[555] Ibid.
[556] World Bank 2014

great estates, and social mobility due to economic change are responsible for this transformation. The key rural politician in these areas is a relatively small landowner (with perhaps 100 acres or so), deeply embedded in the dominant local landowning clan, with influence over the police and administration.[557]Such Landowners are very often local urban politicians too because they own urban property. Nowadays, most of the wealth does not come from the land anymore, but the land is essential links to the people and their votes.[558]

Landownership and the power of kinship are inevitably reflected in the political system of Pakistan. Just as in much of the rest of South Asia, a majority of Pakistan's political parties are dynastic. For many years and particularly after the secession of Bangladesh in 1971, only two parties dominating the Pakistani politics: the Pakistan People's Party (PPP) and the Pakistan Muslim League-Nawaz (PML-N). the PPP is led by Bhutto-Zardari family and has a strong supporter in the Sindhi countryside, while PML-N, which was founded by Zia-ul-Haq, has a very powerful Punjabi character and has been led by Sharif family almost for the last three decades.

Zulfiqar Ali Bhutto came from a family of large Shia landowners who could afford to send him for schooling in the US and the UK. He was very talented speaker. His oratory could manipulate public emotion as the best of Shia preachers could, and his call for social justice resonated with Shia values. His party's flag conveniently displayed the colors of Shiism: black, red, and green. Although he never openly flaunted his Shia background, he commanded the loyalty of Pakistan's Shia multitudes.[559]

The Northern Punjab and the NWFP have less dynastic characters as they have always had a more egalitarian and meritocratic, as with the Pathans and the Jats. In these groups, it is often more accurate to talk of 'big men', risen through personal wealth and character, rather than hereditary leadership. Very often, the decisive moment in family's rise was when they became sufficiently locally powerful to get into a political party as a candidate, and on that basis to get a government job- after that, they can make their fortunes by corruption.

Recently, there has also been a sharp rise in the popularity of centrist parties such that the Muttahida Qaumi Mahaz (MQM) and Pakistan Tehreek-e-Insaf (PTI). The MQM is Pakistan's

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[557] Lieven.
[558] Ibid.
[559] Vali Nasr, *The Shia Revival: How Conflicts within Islam Will Shape the Future* (W. W. Norton, 2006).

only genuinely modern mass political party, which gains support from mostly the middle-class from the ethnic background of the Mohajir population of Karachi. PTI is also a centrist political party in Pakistan founded in 1996 by former international cricket captain Imran Khan. In 2018, PTI or Pakistan Movement for Justice ended the two-party dominance of the PPP and the PML-N by becoming the largest party in the National Assembly as a result of the 2018 general election. As the 19th Prime Minister of Pakistan, Imran Khan is leading Pakistan as a populist, religiously devout, anti-corruption reformist, and envisioning building an "Islamic welfare state". The recent victory of PTI of Imran Khan seems to bring change to Pakistan's political system. However, it is still too early to draw this conclusion. The patterns of political kinship and traditions concerned are very old and very deeply rooted in Pakistani society.[560]

In sum, we may see a conflict of different ideologies, the tension between civil society and military, and fierce confrontation between the Islamists and secular parties within Pakistani politics, however, kinship consideration usually outweighs these differences. Defense of the honor and the interests of the kinship group is often considered to be more important than loyalty to a party, to a state, or to any code of professional ethics, not only for ordinary Pakistanis, but also for most politicians and officials. In Pakistan, waves of public sentiments including Islamic revivalism in many forms can topple regimes and bring new ones to power; but they do not change the basic structure of politics.[561]

Both Pakistan's main Islamist parties today, the Jamaat-e-Islami (JI) nationally and the Jamiat-e-Ulema-e-Islama (JUI) in the Pathan areas, are drawn from the modernist tradition of Deobandi. According to Lieven, the ideological stance of Deobandi can be described as both fundamentalist and reformist. Their aspiration to the pure teaching of the Quran and the Prophet makes them as a fundamentalist group. By its own description, Jamaat-e-Islami is "an ideological party" that stands for "complete Islam" and whose mission, according to Article 4 of the party's constitution, is the "establishment of Divine Order or the Islamic way of life in its entirety, in individual and collective life, and whether it pertains to prayers or fasting, Haj or Zakat, socio-economic or political issues of life." This statement also advocates radical reforms of society.

[560] Lieven.
[561] Ibid.

They are also puritan (in the old Anglo-American sense), in their concern for strict public morality and their dislikes of both ostentatious wealth and the worship of saints and shrines. Their ideas of reform are quite modern, which concerned with questions of modern social justice and development. Majority of their supporter come from middle-class lay intellectuals concentrated in urban centers.[562]

In 1977, these Islamic parties formed the Pakistan National Alliance (PNA) with other political parties to run a political campaign against the left-oriented PPP in the 1977 general elections. This coalition was a populist and consolidated right-wing political alliance, consisting of nine political parties of the country. However, the alliance performed poorly in 1977 general elections. By 1978, the alliance met its end when parties have diverged in each of its agenda. The left-wing parties later would form the MRD alliance under PPP to oppose President Zia-ul-Haq in the 1980s and the right-wing forming the IDA alliance under PML.

The Islamic parties have been consistently participating in the general elections. In the 1990s, the Islamic political parties united on a single platform in 1993 as "Islamic Front" against Benazir Bhutto of PPP and in 2002, they formed another political alliance of the Muttahida Majlis–e–Amal (MMA; "United Council of Action"). Despite its vast mass, populism, and support, the MMA alliance only retained 63 seats while the PPP retained 94 seats and the President Musharraf's PML (Q) securing 124 seats during the general elections held in 2002. In overall, the Islamic influence in the politics has been very limited in the public.[563]

Islam was never enough to make Pakistan into a unified nation. On the contrary, the hostility toward India often provides a better unifying force for its people. This security concern has determined the content and contours of Pakistan's foreign and domestic policy. As a result, this dominance of security policy also paved the way for the superior position of the military within state establishments and society. The Pakistan Armed Forces, the sixth largest in the world in terms of active military personnel and the largest among Muslim countries, have played an influential role in mainstream politics throughout Pakistan's political history.

[562] Ibid.
[563] Ibid.

The Army is also the only institution that has succeeded to some extent in resisting 'feudal' characters of the Pakistani political system in the name of state loyalty and professional meritocracy. However, "It succeeds in part only through turning itself into a kind of giant clan, serving its members' collective interests at the expense of the state and society, and underpinned to some extent by ancient local kinship groups among the north-western Punjabis and Pathans," argues Anatol Lieven.[564] The Pakistani military considers itself as a big family or large kinship group, which maintain its power through extracting patronage from the state and distributing it to its members.

There are longstanding Western fears that the social change in the country will 'Islamize' the Army, which increase their support Islamist revolutions or that there might be a mutiny by Islamist junior officers against the high command. These dangers do exist, but in Lieven's, a Pakistani expert, view, most probably only a direct ground attack on Pakistan by the US could bring them to fruition.[565]

The military officer's ideology was first and foremost Pakistani nationalist. The military tied to Pakistan, not the universal *Muslim Ummah* of the radical Islamist's dream; tied not only by sentiment and ideology but also by the reality of what supports the army. In the 1980s General Zia did undertake measures to make the army more Islamic. Many officers who wanted promotion adopted an Islamic trait in the hope furthering their chances of promotion. However, this did not lead to blocking the career of secular generals from promotion such as General Karamat and Musharraf. In the 1990s, and especially under Musharraf, most of Zia's measures were rolled back.[566]

Pakistan has a complex legal framework, a corrupt police institution, and court system, but a progressive group of lawyers.[567] The Federal Sharia Court (FSC) of Pakistan is the most important institution regarding Islamization in Pakistan. The Federal Sharia Court was established in 1980 during the Zia-ul-Haq regime. It is in the federal capital, Islamabad. The FSC is a prestigious court that has the power to examine and determine whether the laws of the country

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[564] Ibid.
[565] Ibid.
[566] Ibid.
[567] Ibid.

comply with Islamic Sharia law. The declaration of Pakistan as the Islamic Republic in 1953 was also the result of the struggle of these Islamic parties.

It consists of eight Muslim judges appointed by the President of Pakistan after consulting the Chief Justice of this Court, from amongst the serving or retired judges of the Supreme Court or a High Court or from amongst persons possessing the qualifications of judges of a High Court. Justice Najmul Hassan Sheikh is the current Chief Justice of the court in 2017. Of the eight judges, three are required to be Islamic clergy who are well versed in Islamic law. The judges hold office for three years, which may eventually be extended by the President. Related to Islamization program, this court represents the stricter voices of Islamic clergy against the pragmatic approach of the government, the State Bank of Pakistan, or the industry.

The Insurance industry in Pakistan is regulated under the Insurance Ordinance, 2000. The Government of Pakistan established the Department of Insurance in April 1948 within the Ministry of Commerce. The purpose of this arrangement is to take care of affairs related to the insurance under economic and industrial policies. The insurance industry in Pakistan is relatively small compared to India, or even Bangladesh. However, the Pakistani insurance market has undergone significant structural changes in the last few years, particularly, through mergers of companies. According to Insurance Ordinance 2000, an insurance company must meet the increased statutory requirement of minimum paid-up capital. Some companies who were unable to raise this capital have been asked to close their operations. The ordinance increases the efficiency and competitiveness of insurance industry in Pakistan.

Furthermore, the Security and Exchange Commission of Pakistan (SECP), Insurance Division, issues directives on financial security and transparency, code of good governance and sound market practice to boost the industry. The year 2015 showed improvement in Pakistan's overall economic indicators, including containment of current account deficit. However, many argues that this improvement was due to the continuing decline in international oil prices and an uplift in remittances from abroad, and not because the structural adjustment at home.

The successful issue of Sukuk Bond in the international market also helped the investment in Pakistan. Many countries have started to see Pakistan as a potential country for investment. For instance, China and Pakistan made agreements in 2016 to establish the China Pakistan

Economic Corridor (CPEC) between the two countries. As a result, many foreign companies start to open the insurance business in Pakistan. In overall, the Pakistan insurance market is relatively liberalized, with 100% foreign ownership and control of insurance companies permitted. However, in overall the insurance industry has little influence in the regulation of insurance in Pakistan.

Stalling growth and development

Pakistan has been the leader in advocating Islamic finance since its inception. After participating in the establishment of the Islamic Development Bank (IsDB) at the first Organization of Islamic Conference (now called the Organization of Islamic Cooperation) in 1973, the Government of Pakistan initiated a national program to establish an interest-free economy in the eighties. However, this program failed, primarily due to the continuous legal dispute concerning the meaning of 'true' Islamic economy, the shortage of well-trained human resources, and its reliance on the inefficient public institutions.

From the early 2000s onward, Pakistan changed its policy of systemic change of economy. Pakistan has promoted Islamic finance and started a parallel financial system to that of the conventional finance industry. This policy tried to replicate the success story of the Malaysian Islamic economy. By September 2016, 22 Islamic banks consisting of six full-fledged Islamic banks and 17 conventional banks with Islamic banking divisions, five Islamic insurance companies, and 80 Islamic mutual funds are operating in Pakistan. Islamic financial services companies are managing an asset volume of about US$25 (PKR 2,492) billion including 57 *Sukuk* (Sharia-compliant bond) issues with a volume of US$6.3 billion out of which *Sukuk* of US$1 billion matured by September 2013. [568]

In Pakistan, Islamic insurance just started very recently, and at present, only five Islamic insurance companies operate. However, the growth during the period 2009-15 is positive. In addition, assets of the Islamic insurance sector increased by 600% in seven years from PKR2.7 billion in 2008 to PKR16.3 billion in 2015. Currently, these five Islamic insurance companies are

[568] Muhammad Hanif and Abdullah Iqbal (2014), "An Evaluation of Takaful Insurance: Case of Pakistan", *Journal of Islamic Economics, Banking and Finance,* 13 (1). ISSN 2070-4658.

the backbone of Islamic insurance of Pakistan: Dawood Family Takaful Limited, Pak Qatar Family Takaful, Pak Qatar General Takaful, Pak-Kuwait Takaful Company Limited & Takaful Pakistan Limited. Several Islamic insurance models are being implemented by these companies. These include *Mudarabah* based model, which has been adopted by Dawood Family Takaful Limited & Pak Qatar Family Takaful & *Wakalah* Based Model, which has been adopted by Pak-Kuwait Takaful Company Limited.

The reform on the legal framework of Islamic insurance in Pakistan has contributed significantly to its development. As part of the reform, Islamic insurance rules were introduced in 2005. Based on these new rules, Securities & Exchange Commission of Pakistan (SECP) and the Central Sharia Advisory Board are working in close collaboration to aid Islamic insurance companies to provide Islamic insurance services as per Islamic Sharia.

History and development

In 1978 the new president of Pakistan, Zia-ul-Haq, announced the Pakistani government would enforce *Nizam-i-Mustafa*, or the Islamic system. The Pakistani government intended to complete the Islamization process of the country, which had been ignored by the previous regimes. The Islamic system of the economy under Zia-ul-Haq was established through the implementation of Zakat and replacement of interest-based finance to profit and loss sharing system. Pakistan was not alone in conducting this initiative. This decade was a period of the global resurgence of Islamic finance when Muslim countries like Pakistan, Sudan and Malaysia and some Arab countries mobilized their efforts to transform their financial systems on Islamic lines.

The Council of Islamic Ideology (CII) Pakistan was given a task to consider the best strategy to achieve the objective of Islamization. To take help in its task, the CII set up a panel of 15 highly qualified economists, bankers, and financial experts. The panel submitted an interim report, which recommended the immediate removal of interest from the financial institutions whose transaction was relatively less complicated and from where interest could be removed with ease. This recommendation was followed by its final report, which contained detailed

recommendations for eliminating interest from all domestic transactions. The reports were submitted to the government on November 1978 and June 1979, respectively.[569]

Besides drawing some strategies, the Council also examined the laws governing the insurance business in the country. The Council analyzed eleven such laws and expressed its opinion about them in a brief report to the government, which was in March 1984. The Council further decided to constitute a working group to analyze the existing system and frame a new system of surety and assurance following the Islamic teachings. At this time, the Council brought together economists, the heads of the government insurance company and other insurance experts as part of their working group.

The 1984 report of the Council stated the insurance contracts contain prohibited elements including uncertainty in transaction, gambling, and usury.[570] As discussed previously in the matter of prohibition of insurance, the Council also objected the existing insurance contract due to the element of uncertainty of transaction present in the differences between the premium paid and the service received. The Council also considered insurance as gambling in its extreme form. The Council considered those elements come within the definition of unlawful acquisition of others' property. Therefore, the report stated, "insurance in all its forms, except postal insurance in Pakistan, is wrong, wicked, unlawful, prohibited and unenforceable".[571]

According to the same report, cooperative insurance with the following characteristics would be lawful: (i) when an insured is paid a certain sum at the happening of an incidence, the sum paid is considered *tabaru* or donation from all the insured. In such cases, the presence of *gharar* or uncertainty in a transaction is accepted, (ii) as cooperative insurance is not meant to receive profit so gambling and usury will not be present in it, and (iii) the insured are eligible for receiving *qard al-hasan* (benevolent assistance) from the insurance fund.[572] In overall, the acceptance of the cooperative model is due to the social element in the nature of cooperative itself. Cooperative insurance is considered to be closer to the ideal model of Islamic insurance.

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[569] Ghazi.
[570] See Council of Islamic Ideology, *Eleventh Report on Insurance and Laws of Insurance* (Islamabad: Council of Islamic Ideology, Pakistan, 1984).
[571] Muhammad Anwar and Muhammad Hussain, "CII 1984 Comparative Study of Insurance and "Takafol" (Islamic Insurance) [with Comments]," *The Pakistan Development Review* 33, no. 4 (1994).
[572] Ideology. Council of Islamic Ideology, *Eleventh Report*…

Moreover, the Council recommended that the Islamic insurance business shall be conducted by an autonomous, non-profit, state organization. This perspective was like the view of many Muslim scholars in Indonesia, arguing that insurance should be a non-profit endeavor. The insurance fund shall be established as a permanent fund, with the status of a *waqf* (endowment), and not as a business investment. Installments paid by the participants towards short-term general insurance will be added to the Islamic insurance fund. Installments paid for long-term insurance plans will be divided into profit-sharing investment and insurance contributions.[573]

As some of the members of the Council, especially the clergy were strict of the view that the insurance business should be based on mutual help and without any intention of making profit. Therefore, the Council did not find any of the experiences of Islamic insurance companies of that time suitable to be adopted for Pakistan. Majority of Islamic insurance services at that time were provided by the for-profit company from Malaysia and the Gulf countries. The Council was of the view that any insurance arrangement, which was not of the mutual type, will not be acceptable in Islam. Most of the members of the working group agreed that insurance should not be a money-making source for the organizers and should provide cover against those risks only which should be covered in public interest, i.e. insurance should cater to the requirements of the public and not to the requirements of the privileged class. Nevertheless, this effort was discontinued without any concrete policy on Islamic insurance.[574] Besides, the government of Zia-ul-Haq decided to focus on establishing an Islamic welfare system of Zakat and agricultural tax of Ushr. The Pakistan new welfare system was introduced on June 20, 1980, through the promulgation of the Zakat and Ushr ordinance of 1980.

In 1990, a new council came into existence which decided to form another group to complete this task. The working group comprised of six members of the council and four representatives of major insurance corporations. Also, there were around twenty Islamic scholars and insurance experts advising the group on the nature and function of the present system. Their expertise was crucial for the Council to develop an alternative system. The group prepared a

[573] Hanif.
[574] Anwar and Hussain.

report in 1992 and submitted for consideration by the government. In this report, the group reviewed the history of insurance and its present forms. It also investigated the status of insurance from Sharia point of view and found the same conclusion that in its present form, insurance involves the elements of usury, speculation, and gambling.[575]

Like the conclusion of the prior report, the Council report of 1992 had also discarded existing Islamic insurance practices of that time which were considered Islamic alternatives to insurance. The Council reviewed the functioning of Islamic insurance companies, working in different Muslim countries, for developing a practical model for Islamic Insurance and suggested an alternative system based on the concept of *Mudarabah* and *Waqf*. The Council studied STMSB (*Syarikat Takaful Malaysia Sendirian Berhad)*, IAIC (Islamic Arab Insurance Company) and IICS (Islamic Insurance Company Sudan). The Council rejected the IAIC model because, in its view, all conditions of occidental insurance are retained under Islamic nomenclature. The IICS model was also rejected because of the distribution of surplus from the Islamic insurance. According to the Council if the premium is considered debt then all principal amount must be returned, and if it is considered an investment then profits of some participants cannot be diverted in favor of others. As a result, the Council has recommended its model of Islamic insurance which is claimed to be "in complete agreement with Islamic teachings".[576]

The main difference of the report of 1992 compared to 1984 is the Council in its 1992 recommendations showed flexibility regarding private insurance provided the Sharia compatibility of its operations is guaranteed. In the early nineties, there was a huge disappointment toward the performance of state enterprises, including in the Islamdom. State-run enterprises were considered to be inefficient. This fact is apparent from the collapse of the socialist system and the rise of privatization in most countries, including Pakistan. Many proponents of Islamic economy shifted from supporting nationalization to economic liberalization.[577]

The Council opened an opportunity for the private sector to be involved in the Islamization of insurance in Pakistan. The Council recommended that the public sector runs the

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[575] Ibid.
[576] the Council of Islamic Ideology, *1992 'Report on Islamic Insurance'* (Islamabad: 1992).
[577] Tripp.

business of Islamic insurance, so the government may take the responsibility of running this service according to Islamic law as suggested by the Council. If the above requirements can be guaranteed, the Islamic insurance business can also be run by private and semi-government corporations.[578]

The government of Nawaz Sharif of Pakistan Muslim League (PMN-L) had shown its interest towards Islamization of the insurance business in the country and formed a commission to develop a scheme for this purpose. Moreover, in 1993, the government put in place the Sharia Enforcement Act. However, the Islamization Commission's interim report was never presented to Parliament, and plans were never implemented. Like previous effort, despite all elaborations and sophisticated recommendations, there was no practical step has been yet taken for the Islamization of insurance.[579]

Nawaz Sharif won again in the 1997 election and defeated the Pakistan People's Party (PPP) led by incumbent Prime Minister Benazir Bhutto. Sharif was sworn in as Prime Minister on 17 February. Following this victory, Sharif reconstituted Islamization Commission in 1997, drawing largely on the Report of the Self-Reliance Committee, of which Professor Khurshid Ahmad was the chairman. He was the person summoned back by President Zia in the early Islamization program in 1984 with the task of overlooking the Islamization of Pakistan's economy. He was a Pakistani economist based in the University of Leicester who specializes in research, education, and publication, working to advance Islamic economics and Islam in general. He was summoned back from the United Kingdom, and he assumed the position of deputy chairman of the Planning Commission. Professor Khurshid went on to become chairman of the Standing Committee on Finance, Economic Affairs, and Planning during his first tenure in the Pakistani Senate from 1985 to 1997.[580]

On December 23, 1999, the Sharia Appellate Bench of the Supreme Court strengthened the Islamization effort by upholding the 1992 judgment and directed the government to eliminate all forms of interest-based banking by June 30, 2001. The historical verdict consisted of three detailed judgments by Justice Khalilur Rehman, Justice Wajihuddin and Justice Mohammad

[578] Anwar and Hussain.
[579] Ibid.
[580] Alim.

Taqi Usmani. After that things began to change slightly and somehow the Central Bank started to be more supportive toward Islamization of economy and move in that direction and that is how, according to Professor Khurshid, "From 2002 onwards, Islamic banks or banks which would have totally self-contained Islamic units came into existence." He added, "Now, [progress] is very slow, but the direction is correct. Pakistan had two parallel streams, about 90 percent in interest-based and about 10 percent Islamic-based."[581]

The Islamization of insurance efforts gained momentum after the promulgation of insurance ordinance 2000 followed by Takaful Rules 2005 issued by the ministry of commerce (MOC) to regulate the Islamic insurance business in Pakistan. Since then, international players are taking keen interest to initiate Islamic insurance business in Pakistan.[582]

Furthermore, the Islamic insurance business in Pakistan entered a new era in the year 2012. Based on Takaful Rules 2012 issued by SECP, conventional insurance companies can open Islamic insurance window. The Takaful Rules 2012 was a step for promoting the industry rapidly at the national level, and the masses would have an opportunity to fulfill their insurance needs under Sharia.[583]

Many players have become more involved in the development of Islamic insurance in Pakistan. Based on data provided by State Bank of Pakistan (SBP), there were 51 insurance companies (7 life insurance, 39 general insurance, and 5 Islamic insurance), with an asset volume of PKR876 billion (US$9 billion approximately), by the end of December 2015.[584] Assets of the insurance sector have shown a stable growth, with a median of 15%, over the 2009-15 period. The size of the insurance sector is about 3% of GDP (9/271), showing a huge potential yet to be capitalized.

Despite its open and 'liberalized' insurance market, structure of the insurance industry in Pakistan had been highly skewed towards state-owned insurance companies. State Life Insurance Corporation (SLIC) and National Insurance Company Limited (NICL) constituted 74% of the total insurance market, particularly before 2005. Currently, there are five life insurance companies

[581] Ibid.
[582] Akhter and Hussain.
[583] Milliman, *Global Takaful Report 2017: Market Trends in Family and General Takaful*.
[584] SBP, 2016.

and 50 general insurance companies in the country. Most of the companies are private, local, and foreign insurers.

The asset volume of 5 Islamic insurance companies was worth of PKR16 billion (99.5 million USD) by the end of December 2015. The Islamic insurance business has gained momentum in Pakistan after 2005 since the promulgation of Takaful Rules 2005 by SECP. Pak-Kuwait Investment Company (PKIC), a joint venture between Pakistan and Kuwait, started its efforts in 2002 to introduce Islamic insurance in the country. Its major shareholders include Takaful National of Malaysia (25%), PKIC (30%), Meezan Bank (10%) and others (35%). In 2007, a second Islamic insurance company, Takaful Pakistan Limited, started its operations in the country. In August 2007, Pak-Qatar Takaful Group obtained two separate licenses from SECP to start operations in family as well as in general Islamic insurance business in the country. The size of Islamic insurance stream was just about 2% of the insurance sector in Pakistan as of December 2012.[585]

As Malaysia and Indonesia, Islamic insurance products in Pakistan are broadly categorized as family and general Islamic insurance business. In addition, seeing the lower purchasing power as reflected in low GDP per capita and vast population of the rural areas of Pakistan, there is vast scope for micro-Islamic insurance schemes.

Hanif's study presents the growth of assets under Islamic insurance in Pakistan during the period 2009-2015 showing an increasing trend. It shows that the assets of Islamic insurance doubled in three years [2009-11] and were six times more in 2015 than those in 2008. It is important to note that during the seven years period (2009-2015), conventional industry assets increased to three times only, and the GDP growth rate in the country remained below 5%.[586] This trend shows a significant increase in assets under Islamic insurance than conventional insurance, clear evidence of market interest and potential for growth in Islamic insurance in Pakistan.

To conclude, there is an excellent potential for Islamic insurance companies in Pakistan. New rules and policies have been promulgated to develop this industry. The growth and

[585] Hanif and Iqbal.
[586] Ibid.

expansion over the seven years of 2009-15 are very healthy; however, profitability during this period is extremely low. Pakistan’s share of global Islamic insurance for the year 2015 was projected to be US$75 million, which is about 1% of the total global Islamic insurance premium. This proportion still quite small as compared to other countries (e.g., Malaysia, Indonesia, USA, and the UK).[587]

Regulatory framework

Unlike Malaysia, there is no separate regulation for Islamic insurance in Pakistan. Pakistan’s regulatory framework is also different from Indonesia because there are additional regulations for Islamic insurance in Pakistan, whereas in Indonesia, both conventional and Islamic insurance follow the same regulations. Islamic insurance companies in Pakistan must follow both specific regulations on Islamic insurance and general insurance regulation, such as the Insurance Ordinance 2000 and Insurance Rules 2002. These rules regulate all insurance business in the country, including Islamic insurance business. The Takaful Rules 2005 and later the Takaful rules 2012 were however made to provide for the additional requirements of Islamic insurance in Pakistan.[588]

In detail, the Islamic insurance business in Pakistan is regulated by several different regulatory regimes from the rules related to establishing a company in general to the law specifically on Islamic insurance. Islamic insurance companies have to follow legal requirements such as the Companies Ordinance 1984 (SECP-2002); Companies (Issue of Capital) Rules 1996 (SECP-1996); The Insurance Ordinance 2000 (SECP-2011); The Insurance Rules2002 (SECP-2002); The Takaful Rules 2005 (SECP-2005); The Insurance Companies (Sound and Prudent Management) Regulations 2012 (SECP-2012); and Takaful Rules 2012 (SECP-2012). The Takaful Rules cover all aspects of Islamic insurance operations from the nature of operating models to Sharia compliance, qualifications for all persons involved in the business, capital, and corporate governance issues.[589]

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[587] Ibid.

[588] Maryam Dikko and Mahyuddin Abu Bakar, "A Comparative Review of Takaful Frameworks in Nigeria, Malaysia, and Pakistan," *International Journal of Islamic Business* 3, no. 1 (2018).

[589] Ibid.

In Pakistan, the Securities and Exchange Commission (SECP) is the general overseer for both Islamic insurance and conventional insurance operators of the country. As a comparison, the oversight functions for the Islamic insurance industry in Malaysia are performed by the Malaysian Central Bank (Bank Negara Malaysia) and the Islamic Financial Services Board (IFSB). Also, to ensure the exercise of self-regulation within the Islamic insurance industry, the Malaysian Takaful Association (MTA), which is organized by the operators itself, sets a common standard for all Islamic insurance operators to regulate on and control matters concerning the pre-contract examination of agents, agency registration systems, code of ethics, and compliance on Islamic insurance tariffs. In Indonesia, Law number 40, the year 2014 states that the conventional and Islamic insurance businesses are regulated and supervised by the Financial Service Authority (the OJK). However, the specific guidelines for Islamic insurance are provided by an autonomous Fatwa of Nasional Sharia board of DSN-MUI. DSN-MUI is a non-state institution that issued fatwas related to Islamic transaction, including Islamic insurance in Indonesia.[590]

The Companies' Ordinance 1984 governs the corporate sector in Pakistan.[591] To start an Islamic insurance business, a company must register under Companies' Ordinance 1984. According to this ordinance, a foreign Islamic insurance company with 100% ownership can operate in Pakistan by meeting the minimum capital requirement of US$4 million, 50% of which must come from abroad. The minimum capital to conduct life insurance business is PKR500 million, and for general Islamic insurance, it is PKR 300 million, irrespective whether the intended business falls under conventional or Islamic insurance sectors, respectively. Upon incorporation, the company is required to get itself registered under the Insurance Ordinance (2000) with the insurance division of Securities and Exchange Commission of Pakistan (SECP). Section 6 of the Ordinance (2000) provides detail criteria for all registered insurer, which ensures transparency, managerial skills, and justice among the stakeholders.[592]

Also, Islamic insurance company needs to comply with the Takaful Companies' Rules (of 2005 and 2012). These rules allow an Islamic insurance company to provide both for conventional insurance and Islamic insurance. However, the company cannot provide a different product (life

[590] Ibid.
[591] Government of Pakistan, *Companies Ordinance 1984* (1984).
[592] Hanif and Iqbal.

and general). Life insurance must be provided only life insurance Company, which does not provide general insurance product (section 4(2) Takaful Rules).[593]

The Rules allow for both stand-alone and window Islamic insurance operations (Section 3 of the Takaful Rules) even though a window operator is required to display this status below the company name in its place of business and all other relevant correspondences (section 11). Notwithstanding, a conventional insurer may transform itself into an Islamic insurance operator upon application to the Commission and meeting certain requirements set out by the Commission (Section 7(1). In Pakistan and Indonesia, conventional insurance companies can open Islamic insurance window, which is not allowed in Malaysia. In Malaysia, Islamic insurance products can only be delivered by Islamic insurance companies.[594]

Also, the principal operational model of Islamic insurance is *Wakala* (for risk management) and *Mudaraba* (for investment); however, Wakala is also allowed for investment management.[595] Investments must be made according to the Islamic finance principles under the supervision of the Sharia board. the Pakistani framework, though not having specific sections with limitations, in its definition section (section 2 of the Takaful Rules 2012), necessitates the operators to choose between these two models only. Malaysia's framework is more flexible in term of Islamic insurance model compared to Pakistan's model. Malaysia Islamic insurance operators may choose from any of the operating models available worldwide provided the operational model has been approved by its Sharia Committee and Board of Directors, but by virtue of section 8.2 of the Malaysian Guidelines for Islamic Insurance Operation, the approval of the Central Bank must be sought where the Islamic insurance operator wishes to use a model which is to be introduced in Malaysia for the first time. The Fatwa from DSN-MUI No: 21/DSNMUI/X/2001 gives a guideline for Islamic insurance companies in Indonesia to use the profit-sharing model of *Mudaraba*.[596]

Establishment of Sharia board and Sharia compliance audit is necessary. Except for a detailed criterion for liquidation and distribution of surplus in PTF, in the case of ceasing

[593] Dikko and Bakar.
[594] Ibid.
[595] Ibid.
[596] Ibid.

operations, a comprehensive accounting and regulatory framework are being laid down by SECP to regulate Islamic insurance business in Pakistan.[597] The SECP as regulator, has the power to appoint its own Sharia Advisory Board which shall formulate policies and guidelines for Sharia compliance and resolve differences in Sharia rulings relating to treatment of operational issues that may arise amongst Takaful operators Legislation has also included a reference to the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) accounting standards. Additionally, a reference to Sharia-compliant filters for investments is cited.[598]

An Islamic insurance operator is only required to appoint one Sharia advisor, a Sharia compliance auditor, and a Sharia compliance officer. Like in Malaysia and Indonesia, the Sharia committee shall consist of members all of whom must have knowledge in Islamic jurisprudence and/or Islamic commercial law. However, Pakistan has more paper qualification for the committee member. The Sharia advisor needs to have several certifications and degree that show the advisor's knowledge of Islamic finance and Takaful, enough command of the English language and knowledge of Pakistani laws. Moreover, any Sharia advisor needs to have at least four years' experience in giving Sharia rulings.[599] Furthermore, in order to cover further risk, the rules 2012 also mentions about the establishment of reinsurance company for Islamic insurance companies. As there is no local Islamic Reinsurance Company in Pakistan, The SECP has authorized the Pakistan Reinsurance Company Limited (PRCL), a conventional insurance company, to conduct window Islamic reinsurance operations.

There is a considerable difference between Pakistan and the other two countries in conflict resolution mechanism. The Pakistan framework gives authority to the SCEP to sets up a Dispute Resolution Committee via the Small Disputes Resolution Committee Rules 2015. The Committee sits in the major cities of Karachi, Islamabad, Lahore and such other places as may be designated by the Commission and has the power to arbitrate disputes arising from individual life, domestic and motor insurance policy provided the claim does not exceed one million rupees. Also, operators providing micro-Takaful are required to establish an internal dispute resolution mechanism to handle consumer complaints (section 8(4)) of the Securities and Exchange

[597] Ibid.
[598] Ibid.
[599] Ibid.

Commission (Microinsurance Rules) 2013. In Malaysia, the Civil Court under the commercial division of the court, referred to as the *Muamalat* Bench, has been dedicated to solving matters in Islamic financial conflicts. Meanwhile, in Indonesia, the Religious Court has the authority in resolving conflict related to Islamic financial services based on Law number 3-year 2006.[600]

Special features and challenges

In comparison with other countries, there are some unique features and challenges of developing Islamic insurance in Pakistan. Throughout its history over the last four decades, Pakistan has been stressing on developing an 'ideal' and 'perfect' alternative of a model from the Islamic perspective. It has emphasized more on its legal compliance of Islamic law rather than its practicality and economic substance of Islamic economic transaction. The elaborative processes within the Council of Islamic Ideology and public debates on what it means to be an Islamic system had been the primary concern of developing Islamic model of Islamic insurance. One of the indicators of this tendency is its reliance on a good Sharia education and certification rather than finance education in developing its human resources.

Moreover, Islamization intended to have a systemic change within the Pakistani economy. A sectoral reform approach had been accused of "dualism and half-heartedness". This intention of having systemic change had been stumbling block for Pakistan to imitate Malaysian model in the first place. Creating Islamic alternatives within a 'non-Islamic' system was considered by many proponents of Islamic system against the mandate of the Constitution.

Another significant debate in the development of Islamic insurance in Pakistan was the issue on who is the provider of Islamic insurance. Many Islamic scholars argued that the state was the provider of this service based on their interpretation of Islamic law. Being non-profit, mutual, and public had been continuously articulated by the scholars as to the features of Islamic insurance model of Pakistan. Only recently, the scholars have started to accept the involvement of the private sector. They start to mobilize the Pakistani masses in a bottom-up approach towards the Islamic system. Professor Khurshid describes it as the two parallel movements of

[600] Ibid.

top-down from the state level and bottom-up involving and inculcating the private sector, especially the agricultural sector and the cottage industries in Pakistan.[601]

Nevertheless, the current regulatory framework of Islamic insurance in Pakistan relies heavily on the role of the state to provide the guideline, supervise, and resolve conflict. The SECP, which was established in 1999, is the primary regulator and market enabler in the development of Islamic insurance in Pakistan. This centralized feature helps to avoid disagreements in the implementation of Islamic insurance as experienced in the previous decades. However, it also has given an overwhelming burden for this institution. Many critics argue that the SECP has performed well in providing regulations but lack of human resources capability in its overall governance of Islamic finance in Pakistan.[602]

Moreover, private-based Islamic insurance is still considered as an auxiliary of the Islamic welfare system, which has always been promoted by the politicians during each general election. *Zakat* and *Ushr* are still the main tools for the government to give economic assistance to the poor population. In addition, in 2015, Pakistan has launched the Prime Minister's National Health Insurance Program (PMNHIP), which aims to provide health insurance to low-income families in 23 provinces. Through the scheme, they will be given health cards covering them for up to Rs50,000 (US$477) of treatment in public or private hospitals, including emergencies, maternity care, post-hospital treatment and even transportation costs.[603] The Islamic welfare system is still the dominant political program as this program provide a short-term political outcome compared to overhauling the entire social security framework into a more efficient system. This feature will be elaborated further in the upcoming section when discussing 'political life' of Islamic insurance in Pakistan.

In overall market assessment, Islamic insurance business in Pakistan still has a low market share, although growing at a faster pace. The past financial performance appears to be weak, though with significant potential depicted by healthy growth. After the enactment of The Takaful

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601 Alim.

602 Syed Irtaza Ali, "Moral Neutralization in Pakistan 's Capital Markets: A Study of Market Abuse" undergraduate thesis, University of Pennsylvania, 2017.

603 The Economist Intelligence Unit, Pakistan Healthcare: Pakistan launches national health insurance scheme, December 31, 2015. http://www.eiu.com/industry/article/703816654/pakistan-launches-national-health-insurance-scheme/2015-12-31

Rules 2005 and later the Takaful rules 2012, and the establishment of SECP in 1999, Pakistan has a reasonably good regulatory framework in place. Also, the market sentiments are still mixed about Islamic insurance in Pakistan, as many still hardly see the difference between conventional insurance and Islamic insurance.[604] Pakistan's Islamic finance industry in general and Islamic insurance sector in particular needs to educate the public through different venues and platforms about the differences in conventional and Islamic financial industry.

Islamic insurance in a divisive nation

Zia-ul-Haq thought Islam could be a unifying force for the multinational country of Pakistan. However, this state-sponsored Islamization opened sectarian fissures within a far from monolithic Pakistani Islam. Islam was, however, less effective in providing a cohesive national force than Zia anticipated. According to Ian Talbot, one of the prominent historians in Pakistan history, the most significant tension of all was between the state legalistic imposition of Islam and the humanist tradition of Sufism.[605] Although we can dispute the notions of legal Islam vis a vis humanist tradition provided by Talbot, we can agree that 'Islam' is a contested concept in Pakistan. Each Islamist group in Pakistan consciously promote their understanding of Islam as valid Islam.

At the same time, there was no incentive for the government to promote private-based Islamic insurance as the underlying assumption for the state behind the Islamization was having the redistributive policies that can give an immediate impact of growing state's capacity, and by implication, deepen its penetration of society. Islamization in Pakistan's politics can be described as continuous tension between the expansion of state power and social resistance to it.

This section examines coalitional politics behind Pakistan's slow development in Islamic insurance. The main problem for developing Islamic insurance in Pakistan was even though Pakistan is officially an Islamic state; there has been no consensus on how to put Islam into practical programs. The country has been experiencing continuous legal battles over

[604] Hanif and Iqbal.
[605] Ian Talbot, *Pakistan, a Modern History*, Expanded and updated ed.. ed. (New York, NY: New York, NY : Palgrave Macmillan, 2005).

interpretation and bureaucratic neglect by post-Zia administrations who had continued to emasculate Islamization project. Moreover, the obsession of political actors in Pakistan, particularly the Islamic parties, toward the idea of 'Islamic State' as an unnegotiable package of Islamization necessitates all reforms start from and by the state (*étatisme*). As a result, all discussions regarding Islamizing insurance sector in Pakistan had always been translated in the term of the Islamic welfare state. In comparison, the Islamists of Malaysia and Indonesia have been moving from state-centric reform toward the market and civil society channels due to their respective political environments.

Contention over operationalizing Islam

Muslims agree that the Quran condemns *usury*, but do not all agree over what the meaning of the term is.[606] Most Pakistanis agree that usury is any interest on the debt; others believe Quran refers to unethical loans that unfairly enrich the lender and not interest charged under state-regulated banking practices. The economists, bankers, politicians, and bureaucrats who would be responsible to administer the conventional economic system are the ones who usually hold the second view mentioned before.

Meanwhile, Jamat-e-Islami and other Islamist group, with financial support from Saudi Arabia, have advocated the elimination of any interest on the debt and organized numerous symposia to elaborate and develop concepts and practices of the interest-free economy. According to Khurshid Ahmad, the Pakistani intellectual and proponent of this movement, the concept of Islamic economics, including Islamic insurance, is an essential part of the very concept of Pakistan. The Objectives Resolution passed by the Constituent Assembly of Pakistan in 1949, and the Constitution of Pakistan contains essential elements of the vision of Islamic economics.[607] It means there is a mandate to establish an Islamic system of economy. Moreover, the aspiration of establishing *Nizam-i-Mustafa* or Islamic system in Pakistan has always been present in every politicians' rhetoric across the ideological spectrum and throughout Pakistan modern political history. However, the Islamization reforms have had only a minor impact on political, legal, social,

[606] Kennedy, *Islamization of Laws and Economy,* 1996: p.130-1.
[607] Alim.

and economic institutions of the state and Islamic insurance was left far behind. The main reason was the continuous contention over what constitutes Islamization itself.

Muhammad Iqbal and Ali Jinnah provided the imagination of an independent Muslim state and the need to revive Islam as a complete system of life, however it was Sayyid Abul A'la Maududi (1903-1979) and *Jamaat-e-Islami* (established in 1941) who articulated how Islamic revivalism could be brought about in political, social, cultural, and economic arenas. He attempted to make the religion more operational to mobilize the masses. On the Indian subcontinent, Maududi has been hailed as the person who established the economics of Islam as a separate branch of knowledge.[608]

Maududi, the founder of Jamaat-e-Islami, was a journalist and activist who was sympathetic to Indian nationalism initially, but then began to blame nationalism for dividing Muslims. After partition, Maududi chose to come to Pakistan and brought a faction of the Jamaat-e-Islami to Pakistan, and along with other prominent Islamic clergy tried to establish a political role in the new state of Pakistan. Jamaat-e-Islami made the achievement of an Islamic Constitution in the land of Pakistan its central goal.[609]

Jamaat-e-Islami is 'an ideological party' whose mission, according to Article 4 of the party's constitution, is the: "establishment of Divine Order or the Islamic way of life in its entirety, in individual and collective life, and whether it pertains to prayers or fasting, Haj or Zakat, socioeconomic or political issues of life."[610] For Jamaat-e-Islami, being Muslim means both performing the religious rituals and improving the social life.

One of the prominent experts on Jamaat-e-Islami, Humeira Iqtidar, describes this party as a Leninist cadre-based party; Maududi's focus on ideology, ideological training, and structured organizational management with the modernist aspirations of removing the backward traditions, which are considered to be influenced by local customs and feudalism. From its ideological roots, Jamaat-e-Islami moved into a more political phase when Maududi decided that the party would participate in Pakistan's 1958 national elections. However, the party did not gain much political

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[608] Alim.
[609] HUMEIRA IQTIDAR, "Secularism Beyond the State: The 'State' and the 'Market' in Islamist Imagination *," *Modern Asian Studies* 45, no. 3 (2011): 535–64, https://doi.org/10.1017/S0026749X11000217.
[610] Ibid.

success until 1977 with the arrival of General Zia-ul-Haq in a military coup that overthrew Prime Minister Zulfikar Ali Bhutto. With Zia as their patron, Jamaat-e-Islami together with other Islamists group started introducing their concept of Islamization through state's apparatus.

Islamic economics, including the idea of Islamic insurance, grew naturally from the Islamic revival and political Islam such as the Jamaat-e-Islami whose adherents considered Islam to be a complete system of life in all its aspects, rather than a spiritual formula and believed that it logically followed that Islam must have an economic system, unique from and superior to non-Islamic economic systems. According to them, through the Islamic economic system, the gap between the rich and the poor will be reduced and prosperity enhanced by such means as the discouraging of the hoarding of wealth, taxing wealth (through Zakat) but not trade, exposing lenders to risk through profit sharing and venture capital. Islamic system does not allow speculation and other activities that bring benefits to certain individuals and bring damage to the society.[611]

Compared to the Islamic economics version of the Iranian revolution, Jamaat-e-Islami was more relax regarding private ownership. Jamaat-e-Islami were opposing the state's land reform policy and did not support nationalization program. They did not call for public ownership of land and large industrial enterprise. However, they advocated on large public sector and public subsidy policies (utilities, public transport, health care, energy resources such as oil, and unused farmland).[612]

The main achievement of the clergy and the Islamic parties in Islamizing Pakistan's economy was the establishment of the Council of Islamic Ideology (CII) and the Federal Sharia Court (FSC) of Pakistan. The Council of Islamic Ideology was established for the purpose of advising the government about bringing its laws and provisions into conformity with the injunctions of Islam. CII made numerous recommendations that interest should be eliminated in Pakistan as it is forbidden by Sharia.

In 1977, CII was entrusted by the next president of Pakistan, Zia-ul-Haq, with the task of preparing a blueprint for making the economy interest-free. President Zia directed the Council

[611] Alim.
[612] Lieven.

with specific goal of eradicating interest from the economy. As a result, the issue of interest or usury gained central issue in country's policy arena.

As mentioned in the previous section, the Council of Islamic Ideology (CII) appointed a panel of economists and bankers in November 1977 to assist the Council in the delicate task of finding ways and means to eliminate interest from the financial institutions and re-model (Islamize) Pakistan's economy. CII submitted several reports and made several recommendations to transform the socio-political and economic system into a system conforming to the tenets of the Sharia. Those included the reports and recommendations on Islamic insurance as discussed earlier.

The Federal Sharia Court (FSC) was established in 1980 also during the Zia-ul-Haq regime. The FSC office is in the federal capital, Islamabad. It is a prestigious court which has the power to examine and determine whether the laws of the country comply with Islamic Sharia law. Beside these two institutions, the declaration of Pakistan as an Islamic Republic in 1953 was also the result of the struggle of these Islamic parties.

The Islamic parties, including Jamaat-e-Islami have not become the force in politics it had hoped to be and only achieved a minor result in the elections. It is partly because there was no massive support from most of the Muslim population. A majority of Sunni Pakistanis are the Barelvis or traditionalists, which have traditional religious attitudes and resistance toward the modernist agenda offered by the Deobandis group such as Jamaat-e-Islami. Also, Maududi's insistence on a cadre-based system and his desire to control the organization meant that while his writings influenced many and found avid readers across North India, the Jamaat-e-Islami remained a small, relatively tight-knit group for many decades after its inception. Indeed, the Jamaat-e-Islami can be considered as the best example of Leninist party in terms of its organizational structure and modus operandi.[613] Nevertheless, Islamic parties have continued to have an influence in Pakistani politics due to the patronage received under Zia-ul-Haq. The Islamization Program of Zia-ul-Haq, Islamization amendments in Pakistan's Constitution, and the Islamization of the economy are the results of these Islamic parties' efforts.

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[613] IQTIDAR.

On the other spectrum, Islamization was not defined as an establishment of an Islamic state. The aspiration for Islamization was expressed in the leftist idiom of 'Islamic Socialism' and not in term of Sharia implementation in Pakistan. From 1970 to 1977 West Pakistan was under the leadership of Zulfiqar Ali Bhutto and Pakistan People's Party (PPP). PPP advocated a program compounded of agricultural and industrial reform and the promulgation of a new constitution which defined Pakistan as an Islamic socialist republic. The president and prime minister were to be Muslims, and laws were to conform with Islam as determined by the Council of the Islamic clergy.[614]

Zulfikar Ali Bhutto with PPP had laid a foundation to use Islam in addressing the nation's unbalanced economic development. PPP's Foundation Documents, authored by J.A. Rahim and Mubashir Hasan, stated the intention to merge Islam with socialist ideas and liberal democratic values. They claimed that this attempt, of so-called 'Islamic Socialism' would serve the interests of the masses, not the capitalists, it was said, had pillaged the country and left people more destitute that during the period of colonialism.[615]

Moreover, Bhutto attempted to transcend Islam in Pakistan from merely personal piety into a pragmatic religion. For instance, Bhutto interpreted *Jihad* as synonymous with the idea of Islamic Socialism. Jihad was interpreted as applying to everyday human struggle the dedication of abolishing artificial distinctions and making righteousness the criterion of honor among men and establishing a democratic and egalitarian social order.[616] Bhutto adapted socialist expressions of the charismatic Mao Zedong by saying that the party's purpose was social change based on Islamic teachings, not a socialist revolution.

Furthermore, Bhutto used this idea to threaten or reduce the power of his political adversaries, particularly in the metropolitan centers. Thus, Bhutto did not hesitate to nationalize the economy and conduct land reform. Since 1976, Bhutto extended his earlier nationalization program when he ordered the government to take control of all cotton-ginning, paddy-husking,

[614] Talbot.
[615]Ziring and Burki., page 377
[616] Foundation Documents of the Pakistan People's Party, November 1967, p. 7

and flour milling. Bhutto's actions were pleasing to many farmers in the rural areas but generated resentment in the broader public.[617]

Bhutto argued that his Islamic Socialism was not communism. Islamic Socialism acknowledged the right to private property but always be subordinate to the interests of the community. His socialist regime, it was said, would never threaten Islamic tradition, and it was often repeated that no law would be enacted that was repugnant to Islam.[618]

Although he was not religious himself, Bhutto showed his support to Islamic causes by the promulgation of 1973 Constitution. Considering the previous experience, the Constitution of the 1973 was more Islamic in character than the previous ones. Under Bhutto leadership, PPP framed a Constitution that true to the aspirations of people and principles of Islam. The Constitution of 1973 recognized Islam as the religion of the country and enjoined upon the State to serve the cause of Islam and to bring all existing laws in conformity with Islam. The Islamic Advisory Council (later, was re-designated as Council of Islamic Ideology) was set up to recommend ways and means to bring existing laws of the country in conformity with the Islamic principles. The Constitution explicitly requires the state to take necessary steps for the prosecution of social justice, and eradication of social evils, such as prostitution, gambling and taking of harmful drugs, and pornography.

Despite his effort to soften his socialist programs with Islamic idioms, the clergy and the religious political parties like Jamaat-e-Islami and JUP were continue opposing his idea of Islamic Socialism. They argued that Bhutto had the intention to implement his ideas in the same pattern as practiced in China. Bhutto's ideas were also considered to be secular based on Western worldview. At that time, the religious parties had only 18 members in National Assembly, but this tiny group had a stronger voice in the Assembly and support among the population concerning Islamic issues. Many people were convinced that Bhutto economic program as merely an Islam-coated socialism, instead of a genuine Islamization of Pakistan economy.

Despite little success in the general elections, Islamic parties have continued to influence Pakistani politics. This continuous effort obtained enormous support by Zia-ul-Haq who thought

[617] Ziring and Burki.
[618] Ibid.

that Islam could be a unifying force for the divisive nation of Pakistan. After the removal of Bhutto government in 1977, General Zia became the patron of Islamization in Pakistan and for the first time in the country's history, opened the bureaucracy, the military, and various state institutions to Islamic parties.

Islamic reforms accelerated during the beginning of the Zia regime. However, this state-sponsored Islamization opened further sectarian fissures within a far from monolithic Pakistani Islam.[619] Islamization, which means putting Islamic ideas into practical programs, including in economy, received challenges from many fronts.

It was different compared to the Islamization of Iran during the 1979 Revolution. In Iran, the Islamist force agreed to develop a new form of the Sharia that is modern and more adapted to the contemporary world. Meanwhile, there was no consensus like that in Pakistan. The different Islamist groups in Pakistan cannot agree on which form of the Sharia they wanted to implement. There were different structure and process that happened in those two countries. While Iran has a unitary and centralized form of Shia Islam that has been established by an empire for hundreds of years. Pakistan has a diverse form of Sunni Islam and tension between Sunni and Shia Islam.[620] This continuous contention over operationalizing Islam has led the actions of executive authority to postpone several times the project of the complex Islamization of the banking and insurance sectors, and the economy as a whole.

A 'providing state' in an Islamic patrimonial system

Beside the contention mentioned above, there was little incentive for the Pakistani state to support the development of private-based Islamic insurance within a 'patronage to kinship' economy of the country. The underlying assumption behind the Islamization project since the 1980s was in an Islamic setting, state will be responsible for fulfilling the needs of every citizen with enough protection against any worries. "Islamization" of redistribution or the creation of an Islamic patrimonial within a concept of Islamic welfare system has been the state's essential tool in an Islamized national politics. This project brought advantage both to the state and Islamic

[619] Talbott.
[620] Lieven.

groups. Therefore, the redistributive policies such as the implementation of Zakat and Ushr, and not private-based Islamic insurance, were the backbone of Zia's Islamization project of Pakistan.

Zia Ul-Haq regime inherited weak economic indicators from Z.A. Bhutto in term of growing debt servicing and declining GDP growth. However, Zia managed to avert those indicators due to generous western aid to the tune of $ 3.2 billion from the US after Soviet interference in Afghanistan in 1979 and increasing volume of remittances from $ 0.5 in 1978 to $ 3.2 billion in early 1980s.[621] It helped greatly to stimulate growth increase in GDP to 6.6% from 5% during Bhutto period. Under the jargon of Islamization, Zia regime also brought shift form socialist economy of nationalization to capitalist economy. Zia regime gave a major role to private sector in the process of growth.[622]

The government employed and adopted many recommendations by professionals, engineers, and economists to meet the goals of economic reforms. The new policy relied upon building private-sector and enterprises to achieve economic goals. Under a new policy, the private-sector investment grew from ~33% in 1980 to ~44% in 1989.[623] However, Zia's economic development was still dominated by *étatisme*, a policy which started since 1958 emphasizing on the state's dominant role in directing industrialization through licensing practices and subsidies.

Several industries were privatized but not banks and insurance that were kept under government-ownership management. At the time of independence in 1947, 84 insurance companies were operative in Pakistan, but the insurance industry was nationalized in 1972, and merged into State Life of Pakistan and only in the 1990s, the financial reforms allowed private and foreign companies to establish their business in the insurance sector.[624]

The reason for not changing the status quo of insurance was the political importance of redistributive policies for both Zia and Jamaat-e-Islami. Although, Zia's new economic policy focused on liberalization of the economy, it fell under the Islamization program, which aimed for the creation of an Islamic welfare system. The new Islamic ordinances, particularly on the religious taxes which were promulgated since 1979, absorbed the liberalization of the economy

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[621] Hussain, 2004.
[622] Ibid.
[623] Introduction of Structural Adjustment Programme (SAP) in Pakistan: Transition towards Market Economy Isran, Manzoor Ali; Isran, Samina. *Journal of Business Strategies*; Karachi Vol. 7, Iss. 2, (Dec 2013): 73-86.
[624] (Malik, Malik & Faridi, 2011; "State Bank of Pakistan", 2005).

under a new economic system. According to Nasr, these redistributive policies was essential for the close alliance between the military-led by General Zia and the Islamic parties.[625]

Moreover, Nasr argues that the core issue of Pakistani politics has always been the expansion of the (weak) state power and social resistance to it. In "weak state," autonomy of state institutions cannot be preserved, and as a result, industrial policy making and relations between public and private sectors become directly reducible to pursuit of private interest.[626] Redistributive policy is a way for the state to gain power and legitimacy among the people.

In addition, in pre-capitalist society such as Pakistan, redistribution and gift giving are essential in buying political loyalty. As the state of Pakistan has been fundamentally weak since its inception, in order to contend with powerful 'feudal' alliance and other political actors, the state needs to rely on redistributive policies in order to increase its capacity and influences. Therefore, redistributive policies either in the form of land reform, or Zakat during Islamization of Zia-ul-Haq were very significant in strengthening state capacity against those diverse social forces.[627]

In Pakistan, land reform has been the primary vehicle for redistributive policies. Since its independence, the Pakistani state had become dependent on the landed elite and their networks of authority to maintain order in rural areas; so much that they had been integrated into state organization. The state was, therefore, hard-pressed to push through meaningful land reforms. Ayub Khan (1959-69) and Z. A. Bhutto (1971-77) introduced only modest land reforms—after the two land reforms of 1959 and 1972 still 30 percent of Pakistan's farmlands were owned by 0.5 percent of the landowners.[628]

Zia ul-Haq, backed by Islamist parties, opposed land reform programs of previous regimes. Zia needed to find another mean of redistributive policy, which consistent with the ideas and interests of his supporters. As a new military regime, Zia was under pressure from the powerful anti-Bhutto alliance (landowners and the Islamist parties) to undo Bhutto's socialist policies, including land reforms and nationalization. To compensate for this shortcoming, the

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[625] Vali Nasr.
[626] Nasr, Islamization of landed elite.
[627] Vali Nasr, "Islamization, the State and Development", in *Islamization and Pakistani Economy,*
[628] Ibid.

state has sought to promote equity through other channels, including taking over religious lands and endowments, and the collection of religious taxes and distribution of the proceeds. By the end of the 1980s, the distribution of religious taxes approximated the level of all government subsidies, which shows how central Islamization measures have become to the state's redistribution policies.[629]

During the first years of his rule (1977-84), Zia co-opted Islamic forces to balance the power of the landed elite. Zia showed strong pro-Islamic stance by reintroducing traditional Islamic punishments, prohibiting gambling and alcohol consumption, and creating a new judicial review system. Moreover, Zia sought to introduce a number of distributive programs as part of his Islamization package. These were designed both to aid the poor, and to consolidate the state's control over Islamic institutions—a continuation of the policy first introduced by Ayub Khan in 1959. This control would extend the state's presence to the private sphere.

Zia introduced the system of *Zakat*, which is the Islamic requirement that Muslims share their wealth with the less fortunate members of the community. Pursuant to his zakat ordinance, monies derived by the government were to be divided into three parts: a local account, provincial account, and a central account. Such funds were earmarked for community use and were intended to spark development schemes from the village upwards. A hierarchy of control boards was created to administer zakat collections, and Zia also appointed an Administrator-General to oversee the entire program making him directly answerable to the President.

This mandatory religious tax was enforced in 1980, which applied to saving accounts and other investment at the rate of 2.5% per annum. In addition, there was mandatory 10% tax called *Ushr* that applied on the farm harvests and imported products. Ushr laid the foundation for an Islamic welfare state, and that funds generated by ushr would be used to expand Pakistani industry, construct pukka roads, and build modern state-of-the-art hospitals. Also, the monies collected through the Islamization program would help social services for all Muslims, Sunnis and Shia alike.[630]

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[629] Ibid. 92.

[630] Ziring and Burki. 468

However, there was a strong reaction came from the country's Shia community, which claimed that zakat tax was a Sunni Muslim contrivance and that they had their own collection practices. The Shia argued that their religious observances had been undermined by the ordinance, and that it exposed the community to the manipulative capabilities of the majority Sunnis. At the height of the controversy, a Shia group had stormed the Federal Secretariat in Islamabad and had held it hostage for three days when the government refused to answer their complaints. Following that episode, and not wanting to further excite religious passions, Zia exempted the Shia from the otherwise obligatory rule.[631]

During Zia's Islamization, the state coalesces with social force (the Islamists) using Islam as the symbol. For Zia, Islamization of economy was not meant to implement Islamic rulings in economic transaction including insurance, but it was primarily as a disguise of a new redistributive policies. This strategy strengthened the state against the strong kinship networks of the feudal class, and at the same time, presented Zia's government as an Islamic government. As a military officer without feudal kinship support, Zia tried to find support from the Islamic clergy and general public with his Islamic redistributive policies of Zakat and Ushr.

In addition, the state's takeover of the collection and distribution of religious taxes was aimed at improving social welfare, but also to help the government's budget deficits. In fact, since 1988 Zakat and Ushr funds have been officially integrated into the government revenue accounts. In sum, Zia used Islamization more as a strategy to strengthen the state power rather than simply an honest aspiration or reviving Islamic laws in Pakistan economy as the clergy and Islamic parties suggested.

At the same time, the Islamist parties of Jamaat-e-Islami was continuously holding the idea of 'the Islamic state' in their political imagination. It was the imagination of the ability of particular institutions associated with the state in managing and directing individual behavior.[632] Any kind of Islamic reform had to be conducted through the instrument of the state. It is the state and no other institutions, including market, can tackle this task. It is a type of statism, which is the belief that the state should control either economic or social policy, or both, to some degree.

[631] Ibid. 466-467
[632] Iqtidar.

Therefore, controlling the state was the primary objective of any Islamic reforms promulgated at that time.

Zia's Islamization of economy program was translated in as creating welfare system where state will be responsible to fulfill the needs of every citizens with an enough protection against any economic difficulties. For many Islamic intellectuals and activists, it was absolutely unjustified not to term the Islamic state as a welfare state. The economic implication of this comprehensive welfare concept is that the Islamic state is responsible for eradicating poverty and creating conditions for full employment and a high rate of growth and also arranging social security and foster equitable distribution of income and wealth.

The debate within the Council of Islamic Ideology on Islamization of insurance had shown the insistence of the clergy for having the state as the primary provider of economic protection. The Council recommended that the Islamic insurance business shall be conducted by an autonomous, non-profit, state organization. Moreover, they were strictly of the view that the insurance business should be based on mutual help and without any intention of making profit, therefore the Council did not find any of the experiences of Islamic insurance companies of that time suitable to be adopted for Pakistan. The Council was of the view that any insurance arrangement, which was not of the mutual type, will not be acceptable in Islam. Only in the Council's recommendations of year 1992 showed its flexibility regarding private insurance. The Council recommended that the business of Islamic insurance be run by the public sector, so the government may take the responsibility of running this requirements and details according to Islamic law as suggested by the Council. If the above requirements can be guaranteed, Islamic insurance business can also be run by private and semi-government corporations

Besides, the primacy of the idea of Islamic welfare state gave political benefit to the Islamist parties. "Islamization" of redistribution has by itself Islamized national politics to the advantage of Islamic groups. Throughout the 1950s the Jammat-e-Islami helped galvanize support for the landed elite against land reform by underscoring the sanctity of private property. The alliance was able to undo the government's plans. Adversely, the problem of rural poverty and the socioeconomic position of the landed elite too elicited a response from Islamic groups. When Zia took power, Islamic parties rallied behind him to introduce new distribution policies.

Zia included Islamic parties in the drafting of Zakat and Ushr ordinances and gave them access to various state resources. Religious leaders then became one of primary actors in promoting rural development projects and rural development. As a result, the redistributive policies were used to increase popular support toward the Islamic groups and gave these groups more access to the state's policies. However, the reliance on the idea of Islamic welfare state had stalled the development of private sector in Pakistan, thus there were no Islamic insurance companies prior to the year 2004.

The Zakat and Ushr laws may have helped the state's revenues and to a modest extent contributed to its provision of social welfare, but only after exacting a steep political cost in terms of entrenching Islamization in state policy and national politics, fanning the flames of sectarian conflict, and expanding state capacity.[633] Eventually the increase in the capacity of the state through Islamization would also bring about tensions in the relations between the state and its Islamic allies. The Islamic parties were increasingly unhappy with the increase in the state's control of Islamic institutions.

It is important to note that Islamization has been a manifestation of deep-seated struggles between the weak and developing Pakistan state and powerful social forces. As such, Islamization's impact on Pakistan's economy must be gauged in terms of the extent to which it has facilitated the state's penetration of the society and control of the economy.[634] In comparison, Mahathir of Malaysia encouraged Islamic insurance in a way that consistent with Malaysia's economic liberalization agenda. Supporting Islamic insurance was a political way of demonstrating that Mahathir and UMNO remain connected with their constituents' Islamic roots, and at the same time, building a working Islamic insurance-backed economy, especially one without heavy state subsidies, would reinforce the transformation toward a modern and entrepreneurial Malay society. On the contrary, in Pakistan the underlying assumption behind Islamization was having the redistributive policies that can give an immediate impact of growing state's capacity. "Islamization" of redistribution—creation of an Islamic patrimonial and/or

[633] Nasr.
[634] Vali Nasr.

welfare system—has by itself Islamized national politics to the advantage of both Zia regime and Islamic groups.

In summary, the Pakistani state's emphasis on state redistribution by using Islamic institutions reflects its desire to gain public acquiescence to its domination in the same fashion as it has been extended to the landed elite and their kinship network. Domination in pre-capitalist society largely occurred in various forms. It can be in acts of generosity and distribution of resources were reciprocated by loyalty. As the state sought to replace traditional elite, the state was compelled to contemplate a similar normative order, but one in which state institutions would extend generosity and receive loyalty. According to Nasr, as the state of Pakistan implements redistributive policies of religious taxes, and not empowering market through state support of private-based institutions, its capacity grows. By implication, its penetration of Pakistani society deepens.[635]

From failed co-optation to negligence

There were series of attempt to co-opt Islamization ideas and Islamic forces throughout Pakistan history, but all failed. General Ayub Khan and Pervez Musharraf tried modernizing the country by implementing secular nationalist model like Turkish republic. General Zia-ul-Haq made effort to co-opt Islamization demand and unite Pakistan through enforced adherence to a stricter and more puritanical form of Islam mixed with Pakistani nationalism. Zulfikar Ali Bhutto, founder of the Pakistani People's Party and civilian ruler of Pakistan in 1970s, for his part tried to rally the Pakistani masses behind him with a program of anti-elitist economic populism of 'Islamic socialism', also mixed with Pakistani nationalism. [636]

To stay in power Z.A. Bhutto was compelled to devise a new strategy. He actively championed Islamization in the hope of co-opting a part of the opposition. Bhutto made further concessions to Islamic morality, such as prohibiting alcohol and gambling. In addition, he initiated the establishment of the Council of Islamic Ideology under the supervision of Mufti Mahmud. The task of this Council was to oversee the implementation of government-sponsored Islamization.

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[635] Ibid.
[636] Lieven, *Pakistan a Hard Country*.

Indeed, the ‘secular’ government of Bhutto was the one who started the Islamization process in Pakistan. This concession for Islamization was also influenced by the fact of Pakistan became increasingly dependent to oil rich Arab states for loans, commerce, and employment of labor. However, the Islamic parties did not fully support this initiative due to their rejection of the heavy influence of socialism in the practice of Islamization. The PPP eventually was defeated in July 1977 by demonstrations and the intervention of the army.

The new military regime, led by General Zia-ul-Haq (1977-88) and influenced by the Jamaat-e-Islami, again attempted to base its authority on a strong pro-Islamic stance. The government reintroduced traditional Islamic punishments, prohibited gambling and alcohol consumption, and created a new judicial review system. More importantly, the government of Zia-ul-Haq pushed further Islamic economy ideas into practice. Zia introduced the redistributive system of *Zakat* and Islamization of banking system to be implemented in Pakistan.

Zia’s Islamization established approximately 7,000 interest-free counters at all the nationalized commercial banks in January 1980, making Pakistan the first country in the Muslim world with the largest number of Islamic banking.[637] However, although the attempt at the Islamization of the economy was initially started under the umbrella of the constitution, the constitutional authorities were never persuaded to take the implications of these efforts seriously, except in the implementation of religious taxes of Zakat and Ushr.

In 1979, Zia’s government declared that the enforcement of an interest-free Islamic economic system would be completed within a three-year time frame. However, this very same government on June 25th, 1980, limited the jurisdiction of Federal Sharia Court for a period of three years from entertaining any petition to consider fiscal issues including bank interest. With the exception of establishing the Council of Islamic Ideology, the Zia government did not contrive firm provisions and effective strategic policies for facilitating the Islamization process of the economy.[638]

One of the reasons for the lack of support from Zia’s government toward the Islamization promoted by the clergy and Islamic parties was due to the miniscule results by Islamic parties in

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[637] Aurangzaib Mehboob, "Executive Initiative I", *Islamization of* Economy (PDF), Islamic Studies, 2002. pp. 682–686. Retrieved 17 October 2017.
[638] Hanif.

the 1985 national elections. In this election, Jamaat-e-Islami won only 10 of the 68 seats it contested in the National Assembly and 13 of the 102 for various provincial assemblies. With Jamaat-e-Islami proving to be less of a force than expected on the national stage, Zia's support for the party and its Islamization agenda waned.

Benazir, the daughter or late Zulfiqar Bhutto from the left-wing party of PPP, campaigned strenuously against Zia's Islamization both before and after Zia's death in 1988. Benazir criticized the "anti-female" bias in the Zia's Islamization program, and this theme became a major issue of the PPP campaign in 1988. This campaign strategy was successful in bringing Benazir to the power.

Subsequent to the election, however, the issue of Islamic reform has faded from center-stage. Although, her 'anti-Zia's Islamization' campaign contributed to her victory, Benazir's government had done little to hinder the operation of the Islamization as implemented by Zia. Her administration has not dismantled the Federal Sharia Court nor the Sharia Appellate Bench of the Supreme Court.

Benazir's administration was constrained from dismantling Zia's Islamic reforms due to its narrow electoral mandate. She had been well-advised to moderate her opposition to Islamization as directly challenging the reform would entail considerable political costs to her administration. Her administration continued to incrementally emasculate through bureaucratic neglect the already anemic program that she inherited from her predecessor.[639]

Nawaz Sharif became the 12th Prime Minister of Pakistan on 1 November 1990, succeeding Bhutto. The subsequent government manifested a similar attitude except for its establishment of the Commission for Islamization of the Economy (CIE) in June 1991 to promote Islamic Banking. Furthermore, the ruling government of Nawaz Sharif challenged the 1991 FSC judgment on *riba* in the Supreme Court. The government contended that bank interest is not *riba* and that it was utterly impossible to run the economy without interest in present day circumstances. [640]

[639] Charles Kennedy, *Islamization of Laws and Economy: Case Studies on Pakistan*.
[640] Mansoor and Bhatti, page 146.

Islamization, which means putting Islamic ideas into practical programs including in economy, received challenges from many fronts. Between Muslim groups, there has been unrelenting debate on what exactly Islam says on the matters: Zakat, Ushr, Islamic insurance, etc. Furthermore, there has been series of legal battles over the interpretation of Islamic laws. This continuous contention over operationalizing Islam has led the actions of executive authority to postpone several times the project of the complex Islamization of the banking and insurance sectors, and the economy as a whole.

The divisive political environment of Pakistan made the issue of Islamization of the Pakistani economy becoming a very salient policy issue, where a large number of actors feels that the issue affects them, and that the political system is a way to address the issue. Moreover, rather than debating regulation on accounting practices, setting utility rates, and premium rates, the issue is always associated with ideology and political interests. Unlike in Indonesia and Malaysia with their State or Central Bank, there was no institution that strong enough to solve the differences. In Pakistan, the realization of the Islamic economic model was entrusted to the Council of Islamic Ideology, the Ministry of Islamic Affairs, and the Federal Sharia Court, while the State Bank appeared on a roadside of this process and was content with technical functions. This represents the dominance of the *ulama* (Islamic clergy) and Islamist political parties in the Islamization agenda in Pakistan.

Furthermore, a critical study on the performance of Securities and Exchange Commission (SECP) who is responsible to regulate the insurance industry in Pakistan founds that there is evidence of partial degree of institutionalized corruption which led to the questioning the credibility and competence of the Securities and Exchange Commission of Pakistan as their rightful regulator. This shows the high level of distrust toward state institution due to the relationship-based culture that motivates corrupt behavior.[641]

The main problem for the developing Islamic insurance in Pakistan was despite the fact that Pakistan is officially an Islamic state, there has been no consensus on how to put Islam into practical programs. Both Z. A. Bhutto and Zia regimes tried to co-opt the pressure of Islamization

[641] Syed Irtaza Ali, "Moral Neutralization in Pakistan's Capital Markets: A Study Of Market Abuse" (2017). *Wharton Research Scholars*. http://repository.upenn.edu/wharton_research_scholars/154

from the Islamic groups but failed. Pakistani state was too weak to achieve this even if it wanted too-as Zia-ul-Haq's failed Islamization demonstrated. Moreover, the obsession of political actors in Pakistan, particularly the Islamic parties, toward the idea of 'Islamic state' as an unnegotiable package of Islamization necessitates all reforms start from and by the state (*étatisme*). As a result, all discussions regarding Islamizing insurance sector in Pakistan had been always translated in term of Islamic welfare state as history of Council of Islamic ideology has documented. In comparison, the Islamists of Malaysia and Indonesia have been moving from state-centric reform toward market and civil society channels due to their respective political environments.

Beyond the textual argument and ideologies, it was also battling overpower and interests. The post-Zia administrations continued to incrementally emasculate Islamization project as they could not abort it due to its high political cost. Simultaneously, there was no political incentive for government to promote Islamic insurance as it has little political benefit for them. Consequently, Pakistan has been experiencing continuous legal battles over interpretation and bureaucratic neglect of Islamization project until the present. Consequently, the Islamic insurance Industry in Pakistan suffers from absence of standardization that affects their business especially companies with cross-border selling.

Tribal Islam and conservative attitude toward Islamic insurance

This section addresses the issue of why Pakistani society resists Islamic reform or even the best-designed and best-intentioned attempt at reform and positive development such as the establishment of Islamic insurance. There had been constant radical top-down efforts to transform the country. After Jinnah, various leaders came up with their novel ideas of reforming Islam. Ayub Khan introduced 'modern' Islam, whereas Zulfikar Bhutto came up with his version of a 'socialist' Islam. The 'fundamentalist' version Islam became dominant under Zia military regime. Benazir Bhutto came and put down the radical tone of Islamization and introduced the 'compromising' Islam. Lastly, Nawaz Sharif wanted to boost the private sector under the 'capitalist' version of Islam. These leaders tried to improve Pakistan' social and economic

conditions but they could not stay long enough to continue the reform because there was no political support outside their respective feudal and kinship networks.[642]

Like Indonesia, Pakistan has levels of socioeconomic problems which would seem to be a fertile ground for a mass reformist movement in the name of Islam. Also, it has inherited from India before 1947 on of the leading intellectual traditions of Islamist modernism and reformism. However, the 'reformed types' of Islam failed to transform Pakistani society. It is mainly because the Muslims of Pakistan, like other societies in the Indian subcontinent, have tended to remain socially and religiously conservative. Moreover, due to the strength of kinship loyalty, Pakistani society has little incentive to modify their social institutions and religious practices, including embracing an Islamic but novel and private-based insurance mechanism.

This section begins by elaborating the idea of insurance within Pakistani society, and then explore the social stagnation for the reluctance in accepting the modern scheme of Sharia-compliant insurance. The concepts of risk and risk sharing are tied to the values or culture in local worlds.[643] Pakistani society tends to be resistance to any effort of changing their traditional risk management. This part of this chapter focuses on how Pakistani consume, rework, and hesitate to accept Islamic insurance, whereas, the religious conservativeness and kinship bonds play the most critical part in it.

Islamic insurance and the multiple risk managements

About 97% of Pakistanis are Muslims. They also live in a country that claimed to be an Islamic state. Our assumption is Islamic insurance would be embraced by Pakistani society who are seeking for alternative scheme of conventional insurance. On the contrary, Islamic insurance industry in Pakistan took so much time to take off and there were not enough investment vehicles for Islamic insurance companies to invest in. Islamic insurance has been existing for several decades, yet it hasn't grown as quickly as other Islamic financial services. The answer is Pakistanis rely upon channels of social charity, state assistance, and kinship network for their economic protection, and disregard modern scheme of any private based insurance.

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[642] Lieven.

[643] Golomski.

Insurance is a relatively small sector in Pakistan. Insurance is considered as a 'luxury' good and hence is considered for purchase only by those who are wealthy. However, many of these rich families prefer not to use insurance and rather prefer to invest in property and family business as a form of insurance and life cycle risk management. But for some who chose to buy insurance, they tend to choose Islamic insurance over conventional insurance with various reasons. Abdul Wahab's study shows out of 80 respondents 22 are of the view that they have selected the Islamic insurance model because it is Islamic, 16 are of the view that they are using it because of religious reasons while 30 respondents when asked said that, it is because they are personally satisfied with the Islamic insurance on the other hand, 15 are of the view that, they have chosen Islamic insurance because others (family and friends) ask them to choose it.[644]

Private health insurance in Pakistan is underdeveloped. Only about 7% of health financing is through mandatory and voluntary prepaid health insurance. Private for-profit and not-for-profit health insurance schemes are funded through contributions and mainly based in large cities. Large private employers are increasingly buying private group health insurance for their employees. Still, in Pakistan, the health system is dominated by private financing, in the form of out-of-pocket payments, (at 55% of total funding in 2012). This number of private financing was extremely high in global terms (where the average was 21%). It was also well above the 20% limit suggested by the 2010 World Health Report.[645]

The low level of insurance is due to the small effective market size. In the developing Muslim countries like Pakistan, only public sector employees are forced to save in the form of their pension and social security contributions. Pakistan's Public sector employment is tiny compared to the total Pakistan's workforce. As a result, the market size for insurance and related products are restricted to this group. Moreover, like Indonesia, majority of workers in Pakistan work in informal sectors that are lack of insurance protection.

For majority Pakistani, the state's welfare framework has been their primary scheme for receiving assistance. Therefore, the welfare system is entirely to be the buzzword in daily political debate in Pakistan, mainly due to the prevalent poverty in the rural and urban areas. The

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[644] Abdul Wahab, *the scope of Takaful insurance in Pakistani market, 2013.*
[645] Muhammad Ashar Malik, *Universal health coverage assessment Pakistan,* December 2015.

Economic Survey 2018 revealed Pakistan's percentage of people living below the poverty line in 2015-16 is 24.3 percent of the overall population. This number is a radical improvement of the previous decade of 2005-2006 where 50.4 percent of the people are deficient.[646] The rhetoric of 'Islamic welfare state' partly contributed to the victory of PTI party, which brought Imran Khan to the prime minister seat. Imran Khan's rhetoric on the Islamic Welfare State has gained multiple supports, particularly the Jamaat-e-Islami supporters, and people the urban literate population. These urban literates may not agree in the Jamaat-e-Islami kind of Islam, but they are interested in how Islam is being or is going to be promoted to protect the disadvantaged in the community.

Imran Khan's welfare program is a continuation of different types of distributive policies that had been conducted since Pakistani independence. As discussed in the previous section, the distributive policies are embedded in Pakistan as a 'weak' state. Before Imran Khan's program, there have been land reform, Zakat or religious taxes, and the latest, Bhutto Income Support Program (BISP). BISP is funded through the federal budget in 2008 to provide unconditional cash grants to the most impoverished families in the country.

Regarding the religion of Islam itself, the majority of Pakistani Muslims are traditionalists. For Muslim traditionalist, Islam is an individual religious commitment. Their leaders present Islam in devotional rather than collective term, unlike the modernist of Deobandis (including the Jamaat-e-Islami). The modernist group advocates more than a program for an individual spiritual improvement. For Jamaat-e-Islami and their like-minded groups, Islam offers a systemic transformation of the society based on the formal ruling of the Sharia.[647] Islamic economics, including the idea of Islamic insurance, grew naturally from the Islamic revival and political Islam such as the Jamaat-e-Islami whose adherents considered Islam to be a complete system of life in all its aspects. Islam must have an economic system, unique from and superior to non-Islamic economic systems. The modernist Muslims are the ones who are more receptive toward the idea of Islamic insurance, even though, they initially advocated more on public-funded rather than private-based schemes.

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[646] https://profit.pakistantoday.com.pk/2018/04/26/pakistans-percentage-of-people-living-below-poverty-line-falls-to-24-3-percent-economic-survey-2018/

[647] Lieven.

More conservative Salafi have shown less interest in socioeconomic issues, arguing that the Prophet of Islam and his companions did not study `laws` of economics, look for patterns, strive for understanding of what happens in commerce, production, consumption, therefore it is not necessary for contemporary Muslims to put efforts on those matters. Not only conventional insurance, this group not even entertain with the whole idea of Islamic insurance itself. Moreover, they reject the religious argument of Islamic insurance and contend that transaction is unlawful.

The majority of Pakistani Muslims are traditional who reluctance toward Islamic insurance not because of its legal argument, but because the whole idea of Islamic insurance is too modern. For them, the fundamental concept of Islam is on personal and ethical, not the communal-political aspect of Islam. This traditional understanding of the religion is expressed in the social practices of charity. Islam in Pakistan is having effective role in that softening the misery of Pakistan's poor through charity. One of the prominent charity organizations is The Citizens' Foundation, with more than 600 schools and 85,000 pupils. The Citizens' Foundation is a non-religious organization but a majority if its founding members from the business community are practicing Muslims from different strains of Islam.[648]

Charities with a religious character also tend to be more favored and more trusted by the population. Pakistan's most famous private charitable institution by far, the Edhi Foundation, which is non-religious; however, it is led by a very religious individual, Abdus Sattar Edhi. This charity is vital for a country like Pakistan, where public expenditure for social welfare including health sector were only 5% of government expenditure. Moreover, the charity organization usually plays important role where the level of trust toward state institutions is extremely low. Pakistan has one of the lowest levels of tax collection outside Africa, which shows the public's low level of trust toward the state. However, charitable donation in Pakistan, at almost 5 percent of GDP, is one of the highest rates in the world.

Another religious institution that is central for helping the disadvantaged groups in Pakistan is the madrassah or religious school. For instance, the Red Mosque in Islamabad, which was sieged by the police force under the order of Musharraf in 2007, could afford to feed up to

[648] Lieven.

6,000 students. The funding mostly comes from local individual donations and Zakat from abroad. Many people in the oil-rich Gulf States Muslims send zakat abroad - an estimated £50m a year from Saudi Arabia.

The poor Pakistani families prefer to send their children to madrassah even compared to free public school. It is because madrassah is taking care all the needs of their children, not only for their academic need but also for their daily needs. Madrassah removes the financial burden for many poor parents. Report says over 35,000 madrassahs are currently operating in Pakistan, which is very huge for a country like Pakistan. According to a report issued in Karachi, there were only fewer than 300 madrassahs during country's independence in 1947.

These religious institutions are the genuine voluntary sector of Pakistan. While there are some other 'secular' NGOs with linkage to the International aid organization, but many of them are lack of skills and below the standard required by those international organizations.[649] Nonetheless, many foreign aids are controlled by state apparatus or semi-governmental institutions, and NGOs are under state surveillance because of political suspicion.

The other risk management available and used by many Pakistanis is the remittance through an official money transfer or black-market services of *hawala*. Hawala is black market money transfers that can transfer money any amount, to anywhere, in almost no time. Quick, cheap, and paperless, the age-old hawala money transfer is thriving in Pakistan. Millions of emigrants use it to remit their wages to families back home.

This remittance system relates to the strong kinship of Pakistani society. One study examines the relationship between remittance and family member sickness and shows that the level of remittance increases when there is a family member who gets sick. At the same time, the study found no money transfer among the village members. It shows that the risk-sharing happens between individual within kinship networks and not among individual in a similar location. This habit is quite different from the communitarian model happen in many Indonesian villages where geographical proximity and modern association replace many of kinship ties. This issue will be elaborated further in the next section.

[649] Jeffrey Evan Key, *Nongovernmental Organizations as strategic organization: The Politics of voluntarism in Pakistan,* 1990

As mentioned before, Islamic insurance was presented to the public as the 'Islamic' alternative of conventional insurance. Several studies show that many customers in Pakistan choose Islamic insurance because of a religious reason. Ninety percent of the customers come because the service complies with their religious beliefs.[650] However, this appeals only for the well-off individuals in the urban center, which is quite small. Moreover, the survey of 150 life insurance customers conducted by Akhter revealed that majority of the respondents is unaware of Islamic insurance concept.[651] Some of the upper-income group tends to disregard Islamic insurance partly due to their lack of awareness concerning the Islamic aspect of Islamic insurance. Many hardly found differences between Islamic insurance and conventional insurance.

Moreover, the commitment toward Islamic economics among the Muslim modernists does not necessarily lead to actual participation. As comparison, a separate dataset based on interviews conducted in the Middle East and North Africa alone shows as much as 45 percent of the respondents would choose an Islamic product over an otherwise identical conventional alternative. Moreover, these respondents will still choose Islamic products even if it required paying an additional charge equivalent to 5 percent of the loan amount. However, only 2 percent report current use of Islamic finance. There is considerable gap between expressed preferences and actual behavior.[652]

There are some initiatives to promote Islamic microinsurance to the poor population of Pakistan. This service provides life, health, crop and livestock protection, and small-scale businesses, especially for the rural community. However, the population is more interested in participating in the programs conducted by the State and NGOs, and not Islamic insurance companies. Despite the promotion of Islamic insurance from its religious aspect, the general population of Pakistan tend to use more traditional ways, non-market approaches, of risk management. In overall, the economic activities within Pakistani society are more influenced by tribal ethics of hospitality, honor, and mutual help among kin rather than modern and rational profit seeking motive economy.[653]

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[650] Karim Ullah, *service-system design: an Analysis of Shariah Finance in Pakistan,* March 2014.
[651] Waheed Akhter, *Potential of Takaful in Pakistan Operational and Transformational Paradigm,* May 2009.
[652] Demirgüç-Kunt, Klapper, and Randall (2013)
[653] Akbar S Ahmed, *Pukhtun Economy and Society Traditional Structure and Economic Development in a Tribal Society* (London: London, 1980).

How could this happen? The following section elaborates why there is no transformation within Pakistani Muslim society, which resulted in their reluctance in using Islamic insurance. The religious conservatism and the strong kinship bond are influential in the way they manage economic risks.

The stagnation of social reform

Stating Islamic insurance as the Sharia-compliant service does not necessarily change the beliefs and behavior of most of the Pakistan population, which are deeply conservative. Most ordinary Pakistani aspire of the implementation of Sharia, but it is because of the conditions of lack of justice, security, and welfare within the society. People use 'Sharia' as a sort of code for a better, simpler, more equal, more honest, more protective, and more accessible form of the economic system and not so much about the content of the law dealing with the economy. [654] On the other hand, the Islamist political parties have never achieved sufficient political control in the parliament and could not successfully organize a massive movement for Islamic reform. All in all, the Islamic reform in Pakistan is more concern about putting more religious ruling rather than on the actual implementation of it.

This phenomenon of Islamization of economy is not an isolated phenomenon but is closely connected not only to the internal socioeconomic conditions of the semi-feudal Pakistani society. Historically, the scheme of 'Islamization' of the economy was introduced by a Martial Law regime of Zia-ul-Haq in an arbitrary and undemocratic way. It was a political instrument devised by the ruling elites to maintain the status quo, block land other radical social change. However, the conservative forms of Islam play a more critical role in the lives of Pakistanis than the modernist ideas of Islamic reform. Islam in Pakistan is more presented in term of devotional and ethical, rather than in term of political and collective identities.[655]

Furthermore, there is strong tribal nature presented by Pakistani society. To be more exact, the loyalties and social life of the Pakistani people revolves around the sub-ethnic categories of the family and kin or so-called *baradari*. The family is the basis of social organization,

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[654] Lieven, page 125.
[655] Ibid.

providing its members with both identity and protection. Rarely does an individual live apart from relatives; even male urban migrants usually live with relatives or friends of kin. Children live with their parents until marriage, and sons often stay with their parents after marriage, forming a joint family.[656] This kinship relationship defines to whom their children will be married to, to what political party they will vote in the next election, and to whom they will ask for job and help.

According to Lieven, kinship relations play a central role in wealth creation and distribution for a country with low natural resources, such as Pakistan. In Pakistan, there is no 'traditional' source of wealth for elites to control and monopolize, Lieven further explained. The primary way for aspiring leaders to extract wealth is through a control over state. To achieve this end, communal leaders rely on "patronage to kinship" - a basic dynamic of the Pakistani system. This deep kinship, Lieven noted, is an extremely important aspect of society, used to maintain degrees of stability through power structures.[657]

However, patronage in Pakistan should not therefore be the preserve of the elites, and as simply top-down relationship. A mixture of the importance of kinship loyalty and the need for politicians to win votes, and -on occasions-to mobilized armed supporters. Quite poor people can thus form part of 'human resource networks' and mobilize some degree of help or protection from their superior. Even the very poorest in the village often benefit from the *deg* tradition whereby local landowners and big men distribute free food to the entire village to celebrate some happy event, to boost local prestige through public generosity.[658]

People gain access to patronage by using their position within kinship network to mobilize support for a politician who then repays them in various ways when in office, or by using kinship links to some policemen or official to obtain favor for relatives or allies. In certain circumstances, this can benefit the whole village through the provision of electricity, roads or water. The effects on the resources, and on the state's ability to do things are just the same, but more the results are ploughed back into the society, rather than making their ways straight to bank accounts in the West. This is an important difference between Pakistan and Nigeria, argues Lieven.[659].

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[656] Peter Blood, ed. *Pakistan: A Country Study*. Washington: GPO for the Library of Congress, 1994.
[657] Lieven.
[658] Ibid.
[659] Ibid.

Facing with these multiple problems and weak government, the Pakistani population turn to their kin and biradari to support their economy. In theory, members of a biradari are co-residents of a single village. In some areas, however, land fragmentation and generations of out-migration have led to the dispersal of many members of the biradari among various villages, regions, and cities. Patrilineal kin continue to maintain ties with their natal village and enjoy the legal right of first refusal in any biradari land sale.[660]

Members of a biradari celebrate the major life events together. Patrilineal kin are expected to contribute food and to help with guests in the ceremonies accompanying birth, marriage, death, and major religious holidays. The biradari has traditionally served as a combined mutual aid society and welfare agency, arranging loans to members, assisting in finding employment, and contributing to the dowries of poorer families.[661]

Kinship is central to the weakness of the Pakistani state, but also to its stability, above all because of its relationship with class. Because the Pakistani political elites, especially in the countryside, rely for their strength not just on wealth but their leadership of clans of kinship networks, kinship plays a vital part in maintaining the dominance of the 'feudal elites and many of the urban bosses.

By helping to enforce on the elites a certain degree of responsibility for their followers, and circulating patronage downwards, kinship also plays a role in softening-to a limited extent-class domination. Kinship is therefore partially responsible for Pakistan's surprisingly low rating of social inequality according to the Gini Co-efficient. In both these ways, kinship is a critical anti-revolutionary force, whether the revolution is of a socialist or Islamist variety.

On the other hand, urbanization and economic development have given ordinary people in much of northern and central Punjab more significant opportunities to exploit the system for their advantage. The power of the big landowners and tribal chiefs has been much reduced and has shifted to lower and much more numerous strata of rival landowners and local bosses. This situation gives people more chance to extract benefits by switching between them. Urbanization has also reduced the role of kinship, though not as greatly as standard models predict.

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[660] Ibid.
[661] Ahmed.

Lieven argues that a combination of the weakness of the state and the power of kinship is one critical reason why urbanization has had much smaller impact on political patterns and structure that one might otherwise expect. For in the cities, albeit not as much as in the countryside, you also need protection from the police, the courts and political linked urban gangs." Moreover, rather than new urban population emerging, what we have seen so far is vast numbers of peasants going to live in the cities while remaining peasants culturally. They remain deeply attached to their kinship groups. They still need their kinship groups to help them for many of the same reasons they needed them in the countryside. Underlying all of this is the fact that so much of the urban population remains semi-employed, rather than moving into modern sectors of the economy-because these usually do not exist.[662]

Conclusion: contention and conservative society in Pakistan

The underlying assumption behind the Islamization project since the 1980s was in an Islamic setting, the state will be responsible for fulfilling the needs of every citizen with enough protection against any worries. Also, the mandatory systemic change had been the main theme of Islamization of Pakistan. Consequently, there has been continuous tension between the theocratic element of the state represented by Sharia Court and the ruling regimes- after Zia-ul-Haq until the present days. The Sharia Court judgment decreed that the whole economic system must be based on interest-free instruments. Meanwhile, various regimes after Zia-ul-Haq have stalled full application of this order. Multiple ways of delaying implementation and modifying the injunctions have been found. Legal battles over interpretation have been fought and subtle ways found to avoid a clash over the order to convert to an "Islamic economy."

As a social product, Islamic insurance has been promoted as an Islamic alternative to conventional insurance, which considered to be suitable for Islamic society such as Pakistan. There has been a growing awareness among the educated and urban professionals. However, it continuously receives low support within the general Pakistani society. Most people still rely on traditional methods for risk mitigation and financial protection. Moreover, the state, feudal lords,

[662] Lieven.

and tribal and religious communities still hold prominence role in providing that protection. Like Indonesian society, Pakistanis have a low trust in the private sector concerning providing insurance. There is a general agreement, particularly among the *Ulama* (clergy) in Pakistan that the insurance business should be based on mutual help and without any intention of making a profit. Any insurance arrangement, which was not of the mutual type, will not be acceptable in Islam. Therefore, the adoption of private-based Islamic insurance model has not received wide support among the people of Pakistan.

CHAPTER VI

CONCLUSION

The purpose of this research is to understand the development gap of Islamic insurance between Indonesia, Malaysia, and Pakistan. The central question is, why have Islamic insurance systems developed well in some countries, but not in others. Malaysia has shown a significant growth rate in Islamic insurance demand and outpacing conventional insurance, while Indonesia and Pakistan are still standing far behind Malaysia. Previous studies as already highlighted in the introduction and literature review chapters cannot fully explain the reason why the government and its people supporting or rejecting Islamic insurance as an accepted policy and normative practice within the country. This dissertation is the first such comparative study of the political and societal determinants for the development of Islamic insurance in three Muslim majority countries in Asia.

This dissertation draws on secondary works in several other disciplines in order to answer the research question. Not just political science and history, but this dissertation also utilizes insights from anthropology, economics, sociology, and religious studies. The design of this study mostly follows a qualitative research methodology, specifically case study and combines a range of primarily qualitative approaches. It analyzes political parties and coalition platforms, organizations' charters, and press releases to trace contemporary and prior political norms, priorities, and strategies. Ethnographic and historical studies, documents, and secondary sources help to understand the social and cultural circumstances. Quantitative resources, such as survey data and statistics are used when possible. The paragraphs below provide a summary of the findings in more detail, set recommendations for future research, and a reflection on the overall dissertation process.

The elite, the niche, and the neglected

Islamic insurance is part of the whole package of Islamization, which dated back to the 1980s. The global events of the oil boom and the Iranian revolution, and the rise of revivalist

movements within the Muslim societies created a ‘double pressures’ of Islamization demand to the states, including Indonesia, Malaysia, and Pakistan. After several decades of the Islamization process, these three countries have achieved different results in their Islamic insurance development. Upon critical review of the preliminary data, it was discovered that Islamic insurance system in all three countries produced different results not only quantitatively, but also qualitatively.

Malaysia has shown a significant growth rate in Islamic insurance demand and outpacing conventional insurance, while other countries, including Indonesia and Pakistan are still standing far behind Malaysia. In 2015, Malaysia continued to be the largest Islamic insurance market in South East Asia, with a 62% market share and the largest Family Takaful market globally. Indonesia Islamic insurance sector recently has been showing significant growth by having a contribution of 19% of the total regional market. While Pakistan is falling behind with Islamic insurance comprised just about 2% of the insurance sector in Pakistan as at December 2015, this number was still quite small compared to Malaysia and Indonesia within the same year.

Regarding the regulatory frameworks, all three countries have enacted specific laws for the regulation of Islamic insurance though Malaysia has a fully enacted Islamic Financial Services Act while Indonesia and Pakistan have guidelines passed by their respective insurance regulatory body. Malaysia only permits stand-alone (fully-fledged) Islamic insurance operators, while Indonesia and Pakistan are currently still allowing for Islamic insurance window operations.

All three countries insist on the existence of a Sharia supervisory board for an Islamic insurance operator to ensure Sharia compliance. Malaysia develops a sophisticated network of government agencies, businesses practitioners, and religious institutions to create a national platform and standard. Indonesia state provides the necessary legal framework for Islamic insurance to operate in its jurisdiction. However, it gives autonomy to the non-state religious institution of DSN-MUI to give detail guidelines. In Pakistan, the state very much dominates the regulatory process, and there is less participation from the business community and the public at large.

Regarding dispute resolution mechanism to cater to Islamic insurance-related disputes, in Malaysia, there is in a place known as the *Muamalat* Bench in the High Court to entertain such

disputes and a Financial Mediation Bureau that provides arbitration services for disputes arising from Islamic financial matters including those from Islamic insurance. In Indonesia, the religious court has authority in solving any dispute related to Islamic insurance and other Islamic financial related transactions. In Pakistan, though a similar court has not been created the Small Disputes Resolution Committee sits in significant cities and entertains Islamic insurance-related disputes.

Despite the differences in detail numbers, statistic growth, and features mentioned thoroughly in the previous chapters, there is one primary qualitative difference need to be highlighted. Islamic insurance in Malaysia, developed as a systematic national program, has achieved maturity and elite status at the global level. In Indonesia, the service is continually growing but within a limited scope. It is more precise to describe Islamic insurance in Indonesia as a growing niche market. Pakistan's Islamic insurance came later and had slower growth compared to the two countries mentioned earlier.

This dissertation founds that the coalitional politics behind the decision of political actors to embrace and regulate Islamic insurance as a state's policy and the economic ethics of the societies behind their acceptance (or rejection) of Islamic insurance in their daily lives influence the development gap of Islamic insurance between the three countries.

Firstly, both Malaysia and Pakistan chose to co-opt the Islamization agenda. However, they achieved different results. The successful co-optation in Malaysia owed to the ability of Malaysian leaders to harmonize Islamization with economic liberalization, which led to national-wide support on the agenda. Pakistan failed because Islamization was used as an ideological tool by the state to expand state power against social resistances within Pakistani society. As a result, legal battles over interpretation have been fought and subtle ways found to avoid a clash over the order to convert Pakistani economy to an "Islamic economy". Indonesia took accommodation policy as the state had to respond to the growing influence of the Muslim middle class, but at the same time, it was constricted by the pluralistic nature of Indonesian polity. In sum, the country's fundamental political institutions construct these complex bargains made between various groups within each country.

Figure 6-1: The Political Life of Islamic Insurance

country	***the initiator/s***	***State's response***	***State's role***	***Islamic insurance as a political product***
Indonesia	professor-activist	from repression to accommodation	regulator	distributional
Malaysia	The state & Islamic business developer	co-optation	manager	a national agenda
Pakistan	cleric-politician	from (failed) co-optation to neglect	provider	Ideological tool

Mahathir's Islamization has led to state active participation to ensure uninterrupted public support toward the regime and its liberal economic programs. The Islamization was also intended to transform the Malay population's socio-economic condition, but without disrupting the very capitalist structure of the Malaysian economy. From a political perspective, encouraging Islamic insurance has the advantage of demonstrating that Mahathir and UMNO remain connected with his constituents' Islamic roots. In addition, encouraging investment in Islamic reinsurance has strong potential to reassure underwriters, possibly spurring new investment and creating economic opportunities among Malays where Mahathir and UMNO draw the majority of their support. Building a working Islamic insurance-backed economy, especially one without massive state subsidies, would reinforce the transformation toward a modern and entrepreneurial Malay society. Besides the state, the significant actors behind all of these concerted efforts are a group of scholars with impeccable Islamic and technical expertise and pedigrees. They are generally Sharia trained in the Middle East (most often the renowned Al-Azhar University in Cairo) and PhDs in Islamic finance from universities in the West (often Loughborough or Edinburgh), who proudly call themselves "Islamic business developers" and "entrepreneurs."

In Indonesia, Soeharto's Islamization represented the limited role of the state in accommodating the Islamization demand of a group of Muslim modernists in Indonesia, within the context of its multicultural society. The initiative started as a micro-level experiment by a

small group of Islamic economic enthusiast in Indonesian universities influenced by the global spread of critical ideas toward the practices of a secular and capitalist economic development at that time. It was a bottom-up initiative then later accommodated by the Indonesian state during the last phase of the New Order regime.[663] The changing environment of the New Order in the 1990s and afterward has provided a favorable circumstance for Islamic interest to advance their politics as in social and cultural affairs, but it must be emphasized that this does not mean the advance of a single, coherent ideology called 'Islam'. In Indonesia, Islamic insurance is regulated to accommodate the small number of the urban, middle class, and the modernist group of Indonesian Muslims.

Theoretically, the Islamic state of Pakistan should provide the best ground for Islamic insurance to develop. However, the underlying assumption behind the Islamization project since the 1980s was in an Islamic setting, the state would be responsible for fulfilling the needs of every citizen with enough protection against any worries. This assumption has made the Islamists focused more on the creation of an Islamic welfare state, instead of developing private-based Islamic insurance. Also, the mandatory systemic change had been the main theme of Islamization of Pakistan. Consequently, there has been continuous tension between the theocratic element of the state represented by Sharia Court and the ruling regimes- after to Zia-ul-Haq until the present days. Legal battles over interpretation have been fought and subtle ways found to avoid a clash over the order to convert to an "Islamic economy."

Moreover, redistribution policies play a significant role in a weak and patrimonial state like Pakistan. As the state implements redistributive policies, its capacity grows, and by implication, its penetration of society deepens.[664] In overall, the Islamic economy program in Pakistan, including Islamic insurance, would receive enough state support only when it enhances the political goals of the ruling regime.

Secondly, at the social level, the economic ethics of the societies are the reasons behind their acceptance (or rejection) of Islamic insurance in their daily lives. The new Malay class has reshaped 'Islam' as a new entrepreneurial and corporate ethics, which is supportive of the

[663] Indrastomo.
[664] Vali Nasr, "Pakistan: State, Agrarian Reform and Islamization," *International Journal of Politics, Culture and Society* 10, no. 2 (1996).

development of Islamic insurance in Malaysia. Meanwhile, the robust civic tradition in Indonesia has developed a critical attitude toward the private-based scheme of Islamic insurance. Lastly, Pakistan religious conservatism, counter-intuitively, mostly ignore the modern scheme of Islamic insurance.

Figure 4-2: The Social Life of Islamic Insurance

country	***dominant type of Islamic society***	***Trust on private capital***	***Economic ethic***	***values***	***Islamic insurance as a social product***
Indonesia	Civil Islam	Low	Traditional-communitarian	Piety, social responsibility	Moderately accepted with a critical attitude
Malaysia	Market Islam	High	Modern-capitalistic	self-reliant, piety, care responsibility	Highly accepted
Pakistan	Tribal Islam	Low	Traditional-tribal	individual devotion, honor, kinship responsibility	Largely ignored with a conservative attitude

The Malays has re-articulated their *kampong* values-sharing, fairness, equality, and balance- into a modern and entrepreneurial society of Malays. Entrepreneurship has become the primary vector of ethnic, religious, and moral worth, and a test of virtue and modernity among the new Malay middle class.[665] This type of society of market Islam seeks less to create commensurability between Islam and democracy. It is instead designed to merge Muslim religious practice and capitalist ethics.[666] In Malaysia, Islamic insurance has been widely accepted as it represents the idiom for piety, self-reliant, and care responsibility within the family.

[665] Sloane.
[666] Rudnyckyj.

Although, this attitude seems similar to the Calvinist ethics, Muslim scholars in Malaysia argue that Islamic insurance is unique. In general, the revival of Islamic principles in Malaysian Muslims economic life produces new Islamic norms, identities, ethics, and practices that manifested itself in Muslims' engagement in the markets while still maintaining their Islamic ritual devotions and conservative attitude.

In Indonesia, the emphasis on social benefit has been the primary goal of Islamic economy for many activist-minded of the pioneer of Islamic economy. For many Indonesians, the moral concerns such as addressing poverty, inequality, and economic injustice, must be the main parameter of the success of any Islamic financial institutions, including Islamic insurance. Those social justice values, and not merely legal requirements and profitability of insurance are the priority in defining their economy.

At this moment, many Indonesian Muslims are reluctant to support and subscribe to Islamic insurance premium because the model has not clearly distinguished itself as an alternative for capitalism and foreign economic domination. According to many Indonesian Muslims, Islamic insurance should inculcate the spirit of self-help, solidarity, and cooperation rather than mere economic benefits. Therefore, some Islamic insurance companies in Indonesia have been developing insurance-linked products, which combine financial protection with socio-religious investment to attract Muslim consumers. Others set up a collaboration with Islamic NGOs to deliver micro Islamic insurance to the poor population of Indonesia.

As a social product, Islamic insurance has been promoted as an Islamic alternative to conventional insurance, which considered being suitable for Islamic society such as Pakistan. There has been a growing awareness among educated and urban professionals. However, it continuously receives low support within the general Pakistani society. Most people still rely on traditional methods for risk mitigation and financial protection. Moreover, the state, feudal lords, and tribal and religious communities still hold prominence role in providing that protection. Similar to Indonesian society, Pakistanis have low trust in the private sector giving financial protection. There is a general agreement, particularly among the *Ulama* (clergy) in Pakistan that the insurance business should be based on mutual help and without any intention of making a profit. Any insurance arrangement, which was not of the mutual type, will not be acceptable in

Islam. Therefore, the adoption of private-based Islamic insurance model has not received extensive support among the people of Pakistan.

Moving forward

Ira Lapidus once said that the economically defined social classes were relatively less significant. He stated:

> …(historically) the role of indigenous elites, institutions, and cultures in determining the pattern of development must be emphasized because of some important differences between Muslim and European societies. In the 19th and 20th centuries, European societies were to a considerable extent organized in terms of economically derived social classes. In many European countries, bourgeois elites were the principal forces behind economic development, state organization, and world conquest. Industrial working classes were a principal force in production. In Muslim societies, economically defined social classes were relatively less significant. In these societies, the economy was embedded in and regulated by tribal, communal, associational, and state political structures. State elites -and tribal and religious notables- used political power to control land and trading resources and to extract the surplus product of peasants and other producers."[667]

Our case studies confirm this statement. The economically defined social classes were not the dominant actor in the Islamization of insurance in Indonesia, Pakistan, and even in liberal Malaysia. The high degree of modernization through its latest neoliberal economic development does not necessarily remove the communal pattern and state political structure of Malaysia. Some scholars to describe the process introduce the term 'ethnicized neoliberalism'. The government and ethnic collectives continue to strategically use these liberal economic development models for the social and political positioning of these ethnic groups in contemporary Malaysia.[668]

Nonetheless, are there any market systems in the world that are free from any of this distinctive cultural pattern, anyway? In order to exist, the market needs to have certain customs and rules, which then bring identities, norms, associations based on tribal ties, ethnicity, religion,

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[667] Lapidus, page 486.

[668] Cynthia Joseph (ed.), *Policies and Politics in Malaysian Education* (London: Routledge, 2018), page 17-30.

or gender in the process. Islamic insurance is not merely a process of calculating the risks and compensating damage, but it is also a cultural process where people construct the meaning of their faith, fate, and good faith within their social interaction.

Furthermore, this dissertation provides rich, thick description and analysis of the phenomena of Islamic insurance in three countries. Therefore, it cannot generalize the result for broader population. Its reliance on secondary sources has created another challenge. Malaysia has huge resources on Islamic insurance compared to Indonesia and Pakistan. Therefore, more field works are needed, particularly in the case of Pakistan, to expand this research further.

Potentially, future studies can assess other countries using the similar approach. This dissertation links the Islamic insurance development of the three countries to the quality of the prior colonial institutions. As Timur Kuran suggests, there is a need to have more research on Muslim majority countries who escaped colonization, such as Iran and Turkey. [669] Studying their Islamic insurance institutions might bring more insight into the performance of Islamic economic institutions in general. In addition, it may be interesting to deepen our understanding of the nature of religion and risk by making a comparison with other late modernizers with strong religious-based communities such as China, India, and Latin America. This dissertation should inform the scholars of religious studies that the social, economic and political processes can be as important as the religious doctrines in informing the individual decision of participating in any risk management mechanism.

Similarly, this dissertation should convince Islamic economists and Islamic business practitioners that Islamic insurance is a complex phenomenon that requires wide ranging intellectual input beyond the confines of business and economics.[670] They should seek for greater inter-disciplinary ties and impact for the socio-historical study of Islamic insurance. The development of Islamic insurance in a country does not only depend on the economic improvement or other macro-economic factors, but also on the dynamic of socio-political environment of the country.

[669] Kuran.
[670] Adam Burgess, *Socio-Historical Life Insurance, 'Moral' Obstacles and Sociology*

For practical recommendation, the supporters of Islamic economic movement might like to design insurance frameworks based on the local political and social circumstances in the light of findings of this study. For some countries, the faith-based non-profit health care ministry in the US may serve as a better model than the current private-based Islamic insurance. Strengthening regulation and empowering the non-profit organizations for a country with strong civic tradition such as Indonesia can be an alternative route for developing an Islamic but also an indigenous mechanism to protect the population against economic insecurity. This strategy may be more successful too for a country such as Pakistan that has strong tradition of charity.

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