

## **CURRENCY TRADING / FX TRANSACTIONS IN ISLAM:**

### **Currency Trading**

In Islamic Shariah, there are two opinions related to nature of currency notes:

#### **1. First school of thought:**

- (a). Currency notes are considered as “Floos” (Metal Coins) of ancient times. Therefore the laws of metal coins will apply in exchange of currency notes
- (b). If the currencies are of the same country, they can only be exchanged in equal terms
- (c). If the currencies are of different countries, they can be exchanged at the market rate. The consideration on one side may be deferred to a future date
- (d). However if the payment is deferred on either side, it must be in accordance with the market rate. This condition is put to restrict the use of this transaction to the genuine needs; otherwise it may be taken as a device to effect interest based transaction

#### **2. Second School of thought:**

- (a). Use of currency notes as use of Gold and Silver. The rules applicable to exchange of Gold & Silver (Bai' Sarf) will be applicable to exchange of currency notes. This view is also adopted by AAOIFI Shari'a standard
- (b). Currency of same country can only be exchanged in equal terms and possession must be at spot
- (c). Currencies of different countries can be exchange in unequal terms but possession must be at spot
- (d). Both parties must take possession (actual or constructive) of the counter-values at the closing of the transaction. The counter-values of the same currency must be of equal amount
- (e). The contract shall not contain any conditional option or deferment clause regarding the delivery of one or both countervalues
- (f). It is prohibited to enter into forward or future currency contracts

(g). Possession may take place either physically or constructively. Constructive possession of an asset is deemed to have taken place by the seller enabling the other party to take its delivery and dispose of it

(i)- A delay in making the transfer is allowed to the institution, consistent with the business practice in currency markets

(ii)- Receipt of a cheque constitutes constructive possession, provided the balance payable is available in the account of the issuer

(h). A bilateral promise to purchase and sell currencies is forbidden. However, a promise from one party is permissible even if the promise is binding

### **Forward Cover**

(a). Forward Cover plays a very important role in facilitating imports and exports

(b). Islamic bank cannot enter into a forward sale/purchase agreement, however, they can enter into a promise to sell/purchase agreement in order to sell/purchase foreign currencies in future

(c). Guidelines issued by Shariah Advisor should be followed at the time of execution of these transactions

## **FX Transactions (Shariah Definitions)**

### **Spot (Ready) Transaction:**

If the Deal (transaction) Date & Maturity Date is same then the transaction will be considered Spot (hand-to-hand) as per the rules of currency trading in Shariah. In this case the bank is allowed to do a normal sale/purchase transaction of currency.

### **Forward Transaction:**

If the Deal Date & Maturity Dates are different then the transaction will be considered as forward as per the rules of Shariah (even though the market convention defines Spot transaction in range of 1-3 days under T+2 system). In this case MBL will enter into a promise to Sell or Buy with the counter party.

Hence, all FX transactions that are not 'ready', can only be done on the basis of "Promise to Sell/Buy". This means that those spot transactions which are not settled on the same day will also be done through a promise to buy/sell.(a). Forward Cover plays a very important role in facilitating imports and exports