

THE POTENTIALS OF MUSHARAKAH MUTANAQISAH FOR ISLAMIC HOUSING FINANCE

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SHARI'AH-COMPLIANT



MUSHARAKAH
MUTANAQISAH



BANKS



EQUITY CAPITAL
FINANCING

INTRODUCTION

- Over the years, Islamic banking and finance industry developed several modes for financing.
- One such instrument is known as musharakah mutanaqisah (MM).
- MM or partnership culminating in ownership is a recent innovation in Islamic banking industry.
- MM could be considered as a derivative of original musharakah and ijara modes of financing.
- MM consists of three portions:
 - Musharakah (partnership) between the customer and the bank.
 - Implemented through the contract of ijara between the customer and bank.
 - Customer will continue to buy the shares of the bank gradually until the house is fully owned by him.

OVERVIEW OF MM

Definition



A diminishing partnership whereby a product/project becomes fully owned by a client (Bendjilali & Khan, 1995).

Legality of MM



- It is fully in line with *Shari'ah*.
- Consists of several contracts namely *musharakah* (partnership), *ijarah* (leasing) and *bay'* (sale).

Termination of MM



- A unilateral contract that can be terminated at any time by any party involved.

Salient features of the MM



- Creation of joint-venture between the client and the bank on the basis of *musharakah*.
- Profits are to be shared in accordance to the agreed ratio, but the losses are to be shared in proportion of capital invested by each party involved.
- There should be unilateral, binding promise by the financier to sell his shares of the partnership on instalments.
- The client voluntarily buys the shares of the financier which are to be priced at the market value at the time of the sale.
- The sale component of MM contract is binding only on the financier.

ADVANTAGES OF THE MM

- A relatively cheaper or more affordable mode of finance for asset acquisition in general and home financing in particular.
- The period for financing can also be relatively shortened.
- The financing and the payment of the instalments as well as the rent can be adjusted periodically to reflect the market changes.

DISADVANTAGES OF THE MM

- It is less attractive for the banks since the MM would bring lower profits to the Islamic banks.
- Since the rental price do change over the time and is dictated by the location of the property (in case of home financing), keeping track of these changes may not be an easy job for the banks.
- Legal amendments may be needed especially with regards to the tax structure.

CONCLUSION

- The MM is an equity-based financing technique available for Islamic banks.
- This model can be easily applied in various sectors such as housing projects, financing car purchases, financing working materials and equipments, financing business projects, etc.
- This mode would offer relatively cheaper financing to the customers and help them fulfil their needs in an easier way while complying with the teachings of *Shari'ah*.
- MM is a better solution for the Islamic banks to serve the needs of the Muslim Ummah.

