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Transcending the Trend of Financialization: The Heterodox vs. Islamic Economics View

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Abstract. The paper aims to link three prominent issues relevant to the financial world today – the mounting level of *financialization*, heterodox perspective on functionless investors, and compatibility of Islamic principles to heterodox thinking particularly in regards to interest and uncertainty. Examining the vast array of burgeoning literature the paper argues that the trend of financialization in the capitalist countries has created a new class of capitalist with huge accumulation of wealth ensued merely from financial transactions. Income gap between the rich and poor has widened which is at odd with heterodox perception of equality among social classes. In the Marxian and Keynesian traditions, there is little room for functionless investors to expropriate surplus earned by working and entrepreneurial classes particularly through financing means or rent. We find Islamic prohibition of interest and uncertainty compatible with this heterodox thesis. Islam does not allow rentier income from interest; rather it encourages profit and loss sharing financial contracts so that uncertainty involving with the future income is shared by contracting parties.
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1. Introduction

The words 'neoliberalism', 'globalization' and more recently 'financialization' are commonly used to characterize the change the world has been undergoing over the last few decades (Foster, 2007; Epstein, 2005). Specially, after the bubble burst in the US housing and stock markets which resulted worldwide financial crisis, scholars are paying greater attention to dissect the role of finance in creating and maintaining a new form of capitalism called financialization. The term 'financialization' can be defined as a pattern of accumulating profits through financial channels rather than the traditional means of trade and commodity (Krippner, 2005) or a shift of economic epicenter from industrial to finance capitalism (Foster 2007). Owning to its greater presence in every sphere of economy, financial market has become the pace-setters of all markets as wealth effect, positive and negative, play a crucial role in economic cycle, in

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which 'gambling with analysis, advice, appraisal, advertising, and commission-charging becomes a major growth industry' (Dore, 2000:6). Moreover, finance as capital input for the productive economy is no longer dominant; rather it has been transformed into a mechanism which helps capitalists establish greater influence on economic policies and outcomes for accumulating their wealth.

Wealth concentration through financialization invites many adverse social consequences including inequality and unfairness. Stiglitz laments the current high level of inequality that has emerged in a capitalist country like USA. He reports that while some thirty years ago the top one percent of income earners received only 12 percent of the nation's income, the disparity has grown so dramatically that by 2007 the average after-tax income of the top one percent had reached $1.3 million, but that of the bottom 20 percent amounted to only $17,800. It implies that "the top 1 percent get in one week 40 percent more than the bottom fifth receive in a year" (Stiglitz, 2012: 4). Stiglitz (2012:8) further notes 'both the magnitude of America's inequality today and the way it is generated actually undermine growth and impair efficiency. Part of the reason for this is that much of America's inequality is the result of market distortions, with incentives directed not at creating new wealth but at taking it from others'.

Wealth creation requires investment in real economy. However, the process of financializationhelps elites accumulate huge pile of capital from financing activities rather than investing in traditional production and investment in tangible assets. In the Keynesian perspective this capitalist class can be termed as 'rentier' or 'functionless investor' who '… generates income via his ownership of capital, thus exploiting its "scarcity-value" (Epstein & Jayadev, 2005: 48). They tend tosqueeze those living at the bottom of population pyramid constituting the foundation of consumption and expenditures. Declining income for the bottom class means declining expenditure for consumption goods leading to further reduction of investment in the real economy. Rates of employment and wage fall as a result. Maintaining the consumption level withdeclining absolute wage requires debt to incur at both national and individual levels. A growth regime that relies heavily on debt critically undermines its own liquidity and solvency leading to a vicious cycle of 'systemic fragility' due to Keynes and Hyman Minsky. The current financial meltdown triggered primarily by US subprime mortgage crisis is the inevitable result of increased trend of financializaton (Lapavitsas, 2009). Describing this crisis a 'marginal moment', Sotiropoulos et al. (2013) urge economists to rethink about the workings of contemporary capitalism. Notwithstanding, it seems that our economic society has not yet come towards the feasible direction for transcending capitalism, in particular, transcending the trend of financialization.

In this paper, we take the view of heterodox school including the economics of Keynesain, Post-Keynesian and Marxian traditions to describe the elements and process of financialization and its perilous effects on real economy. Heterodox school is very concerned about social justice of tackling our economic society's arbitrary and inequitable distribution of wealth and income. The school believes that financialization in the capitalist economy will eventually lead the emergence of a capitalist or rentier class that will focus on accumulation by fostering financial profit at the excuse of scarcity of capital (Lapavitsas,2011). Consequently, investment in the real sector will decline leading to poor performance in output and growth. This implies that functionless investors will gain at the expense of other classes in the production system (labor, managers, and entrepreneurs) resulting social inequality and unrest.

Keynes (1936: 344) argues that 'the owner of capital can obtain interest because capital is scarce… but there are no intrinsic reasons for the scarcity of capital.' For Keynes, interest cannot be the price of financial capital because the rate of interest depends on the monetary supply and the demand which is based upon (1) the income level and (2) the liquidity preference of holders. Therefore, interest can be kept at a minimum level, even zero at the extreme case, if a state of full employment is realized. We show that these heterodox traditions have compatibility with the principles of Islamic finance. Islamic prohibition of *Riba*and *Gharar*is an important tool for taming down the wild nature of financialization and its increased focus on rent-income. Moreover, Islamic financing system provides very limited scope for functionless financiers to be benefited from guaranteed income without sharing risk associated with investment.

The paper has been structured as follows: section two briefly describes the process of financialization and its aftermath reflecting the current financial crisis. Section three examines the heterodox view on financialization and its prescribed mechanisms to neutralize the trend of financialization. Finally, section four checks the principles of Islamic finance and its compatibility with the heterodox view which is followed by concluding remarks.

2. The Financialization

Daniel Bell (1973) indicated, in the early of 1970s, the imminent shift of society from the traditional mode of production and distribution to a new form which he termed 'post-industrial' society. The society can be characterized by the emergence of a new class of ruling elite who will be able to establish influential power on economic policy-making. Moreover, the focus of economic activities will be shifted from primary or manufacturing to tertiary sector; therefore, service is considered the *modus operandi* in the post-industrial society which gradually takes the place of industry as the engine of growth. The supremacy of service over other spheres of economic activities will provide finance a competitive edge and greater scope to grow. Capitalizing on this opportunity the rentier classwill emerge who are basically the owners of financial firms and holders of financial assets.

Financialization, particularly in the capitalist countries, began to grow at a noticeable scale in the final quarter of the twentiethcentury when industries in those economies faced tremendous competitive pressure from rest of the world owning to the nascent pace of globalization (Arrighi, 1994). In response to this threat and a way of boosting their already declining profit due to competition, firms started shifting their investment and operations from production to finance. This transformation has bestowed rentiers with enormous influential power over regulatory authority to mould economic policies and structures for their interests (Jayadev & Epstein, 2005). Monetary policy was the key target to functionless investors through which they were able to keep the real interest rates high aiming at reducing budget deficits to curb inflationary pressure and repressing labor force that threatens to limit their share of rents. Kalecki (1943:325) argues that if the government aims for an expansionary monetary policy to maintain the high level of employment 'a powerful alliance is likely to be formed between big business and rentier interests, and they would probably find more than one economist to declare that the situation was manifestly unsound.' In such a way they have successfully promoted financial liberalization yielding them more room for making profit at home and abroad.

Economic and financial deregulation was followed by an increased involvement of corporations with borderless transactions including international borrowing and lending. These transactions are associated with greater risk of foreign exchange and interest rate fluctuations. Thanks to financial innovation, institutions involved with such transactions found a way to replace traditional mode of originate-and-hold financing with new originate-and-distribute technique. Lending institutions, insurance companies, brokerage house, hedge and private equity funds, mutual and pension funds packaged and repackaged certain pools of financial assets by slicing and tranching them into new securities and issued to investors with surplus funds. This easy originate-and-distribute notion of lending and borrowing facilitated credit expansion to such a level that many economies did not afford to sustain the heat. Foster (2007) notes that the US debt in 1985 estimated to be twice of GDP which rose to three and half times merely two decades letter. Once the prime lending market became saturated, financial institutions started extending long term credit to non-prime borrowers forgetting fundamental uncertainty associated with movement of interest rate. Moreover, the originate-and-distribute concept of financing made it very difficult for regulatory authority to trace credit risk for framing appropriate countermeasures.

The growing pace of financialization helped financial industry contribute a larger share of the national GDP while accumulating their wealth through profits from interest, dividends and capital. Dore (2008) shows that the profit earned by the US financial corporations as proportion to national income averaged 9.5 percent during 1950s which rose to 45 percent in 2002 and it continued growing at an average of 16.7 percent annually between 2000 and 2006. In the similar fashion, income from financial activities has outpaced the real income (income from production and manufacturing) for all developed nations. Epstein & Jayadev (2005) report that between the 1960 sand 1970s, on the one hand and the 1980s and 1990s on the other hand,rentier shares of national income made a significant increase in most of the OECD countries. Besides financial institutions, participation of non-financial institutions in financial activities has increased significantly which eventually hastened the speed of financialization. Moreover, they played double roles here - derived profit from financial activities as well as paid substantial portion of their total expense in the form of interest, dividends, and share-buy-backs. Crotty (2005) finds that the payments to financial sectors (interest, dividend, and share buybacks) by non-financial firms as a proportion to cash flow accounted for 20 percent in 1960s and 30 percent in the 1970s 75 percent (at its peak) in 1990. As the cycle goes on gearing up more financial activities and profit thereof, available funds for investment in tangible assets are drained from real to financial markets. Moreover, financial innovation including options, swaps, futures, forwards and other toxic intangible derivative products most of which are over the counter (OTC) traded derivatives made the financial markets more attractive to both financial and non-financial firms. Crotty (2008) shows that the notional value of all derivative contracts rose from about three times of globalGDP in 1999 to over 11 times in 2007.

Of course, functionless investors depend on people engaged in productive activities for their income and wealth (by dint of ownership, lending, and such other means). As such, the former, powered by shareholders 'value-maximization' proposition aiming at reducing principle-agent problem, creates remarkable pressure on the latter to increase and distribute profits. The fundamental concept at the core of agency problem that shareholders of modern firms are dispersed and firms run by professional managers has eroded in the age of financialization. Instead, institutional shareholders have taken their place with their growing presence in the financial markets. Jacoby (2008) explains the growth of institutional equity holding in the USA showing that in 1960 institutional investors owned 12 percent of equities which rose to 45 percent in 1990 and finally peaked at 61 percent in 2005. In 2007, institutional shareholders owned 68 percent of the 1000 largest US corporations (Jacoby, 2008).

Large amount of corporate shareholding by pension funds, mutual funds, private equity, and insurance companies has bestowed them with enormous power and latitude to exercise more pressure on corporate management than ever before. This tension, in turn, forces corporate manager to focus intensely on profit maximization. To attain the desired objective, managers sometimes shy away from long term investment in the real sectors which offers meager return and rather search for scopes and opportunities that will help boosting firm's bottom line even in the short-term. Stockhammer (2012) shows that investment to operating surplus declined in major developed countries during the last three decades which he attributes to the shareholder value orientation and increase uncertainty. Moreover, managers attempt to shed off underperforming branches of the firm in attempts to raise the networth of the corporation and other restructuring activities including mergers and acquisitions, hostile takeovers, leveraged buyouts as well as the outsourcing of productiveactivities (Davis et al., 1994). Profit earned by these means ultimately goes to wealthy accumulators. Foster (2007) reports that the top one percent holders of financial assets in the USA hold more than four times of as much as the bottom 80 percent holders. He further asserts that shareholding by nation's richest one percent of the population is estimated to be equal to the shareholding of the remaining 99 percent.

Moreover, a larger pie of the profit earned by corporations goes to the pocket of firms' top executives in the form of incentives and bonuses. Crotty (2008) shows that top executives of many banks and other financial institutions materialized lavish pay even at the time of crisis when many workers lost their means of livelihood. This proves that the victory of the rentiers has come at the expense of wage-earners and households, who have faced stagnating real wages and increased indebtedness. Stockhammer (2012) reports that the median weekly wages in the United States have grown by a mere 2.8 percent from 1980 to 2005, the bottom quartile of wages fell by 3.1 percent and the top10 increased by 21 per cent. Like USA, real wage has been falling across Europe as well as in Japan. Skewed distribution of income and wealth results social inequality leading to a fragile and unsustainable economic system. Thus, the influence of functionless financiers who accumulate wealth merely through financing means should be curbed to a reasonable extend to avoid those undesirable social consequences. The question is how? Heterodox school provides an important insight toward the issue.

3. The Heterodox Perspective on Financialization

Contemporary heterodox approaches are very much concerned about the rising predatory version of capitalism and its embedded tendency towards crisis. Economists believing in this school cast shadow on the capitalist society where successful participation in social affairs depends less on a person's abilities and skills and more on possession of money-

> Modern capitalism has become a complex game, and those who win at it have to have more than a little smarts. But those who win at it often possess less admirable characteristics as well: the ability to skirt the law or to shape the law in their own favor: the willingness to take advantage of others, even the poor; and to play unfair when necessary. As one of the successful players in this game put it, the old adage "Win or lose, what matters is how you play the game" is rubbish. All that matters is whether you win or lose. The market provides a simple way of showing that - the amount of money that you have (Stiglitz, 2012: 37-8).

Differentiating itself from the dominant neoclassical thesis, the heterodox school explains economic system by its relationship between and among parties engaged in producing goods and services for society '... to meet requirements of those who participate in its activities' (Lee, 2009: 8). The participatory groups are productive classes comprising of entrepreneurs or top managers and workers or earning class. Marx is very outspoken about class system and its indispensible outcome to the society. He explains a state of production as mixed of dead and living labor. The former is the labor embedded in the means of production and the latter expended by workers during the production process. The dead labor, in the Marxian tradition, appears as an alien and hostile power as capital but eventually establishes its overall dominion on living labor. The superiority of capital over labor facilitates the exploitation of labor by capital. Marx states that labors' economic circumstances or sometimes economic coercion forces them to accept the subordination to capital. Economic coercion might construe the abuse of worker's own rights on his labor because capitalists not only appropriate part of what the workers have produced but also abrogate their freedom and autonomy. In Marxist language, dead labor dominates living labor at the end (Elster, 1986).

For Marx, a person is exploited if he performs more labor than is necessary to produce the goods that he consumes. If he actually produces his own consumption goods, the criterion for exploitation is simply whether he also produces goods to be consumed by others. This scenario is captured by his labor theory of value. *The rate of exploitation* is considered as the ratio S/V, where S represents *surplus value* which is the difference between the value the worker produces in a given period and the value of the consumption goods needed to sustain him/her for that period, V represents *variable capital* which is the labor value of the labor power of the workers employed in the production process. In Marx's view, the labor power of the worker is produced out of the goods he/she consumes, therefore the labor value of his/her power is defined by the labor value of these goods, which he/she consumes in fixed proportions just as production takes place with fixed proportions of inputs (Elster, 1986, p. 67). *Constant capital* denoted here as C is the labor value of non-labor means of production, such as machinery, buildings, raw materials that have already been refined by labor. *The organic composition of capital*, a rough measure of capital intensity, is the ratio C/V. *The rate of profit* is the ratio $S/(C+V)$. Dividing the numerator and the denominator in the rate of profit by V yields: the rate of profit = (S/V) / (C/V +1). Or in other words, the rate of profit = the rate of exploitation/ (the organic composition of capital + 1). The tendency of capitalists to substitute dead labor for living labor to increase profit will necessitate the innovation of labor-saving technology. Innovation to be labor-saving means that there is an increasing organic composition of capital. This follows that capitalist must increase the level of exploitation (called as the rate of surplus value mainly including interest and rent) to avoid any decline in profit in the Marxian equation or it should be increased to revert the trend of profit upward. This implies that increasing exploitation is considered one of core processes in the mode of capitalism in the Marxian tradition.

Marx further notes that a capitalist society is featured by the main relationship of exploitation and class between worker and capitalist. In societies where this is an example of dominant relation, there exists a relation of indebtedness arising in the credit market. Marx argues referring to the pre-capitalist society that the class struggle resulted from the conflict between debtor and creditor. The usurer's capital which has the mode of exploitation of capital without its mode of production was pervasive in that stage of society (Elster, 1986: 86). However, the trend has been continuing at an increasing pace and becomes the fundamental building block of financialization in the modern capitalist world. Exploitation through usurer's capital or financial capital, according to Marx, gives no impetus to the development of the productive forces. A functionless investor has neither the incentive nor the opportunity to improve the methods of production because he is not the residual claimant. From this perspective, Marx argues that it is unfair that some should be able to earn an income without working, whereas others must accept the toil of hard work. Capitalist extraction of surplus value is therefore equivalent to theft, embezzlement, robbery, and stealing (Elster, 1986: 95).

Like Marx, Keynes argues that usurers or the suppliers of capital retain the cumulative oppressive power and uses it to exploit the scarcity-valueof liquid capital (Keynes 2008: 344). For Keynes, economic growth could be better satisfied if capital ceases to be scarce. If so, interest rate cannot be considered as the price for supply of capital. He establishes the relationship between savings, investment, and rate of interest stating that saving depends on the level of investment which in turn, depends on the rate of interest (Minsky however, points out that Keynes misses two important elements – asset price level and financial commitment by financial institutions- in determining the demand for money). To achieve full employment by ensuring sufficient investment, Keynes advocates for realization of a *low* rate of interest '… it is to our best advantage to reduce the rate of interest to that point relatively to the schedule of the marginal efficiency of capital at which there is full employment' (Keynes, 1936: 343). The question is: how low should be the rate of interest? Should it ultimately be zero?

From the perspective of Keynes, the answer is affirmative, provided that the low rate of interest brings full employment. According to Keynes, the scale of investment depends on the relation between the rate of interest and the schedule of the marginal efficiency of capital. In theory, a lower rate of interest, zero rate of interest at the extreme case, would encourage the borrowers (mainly enterprises) to make more investment so far as their prospective yield of the investment remains unchanged (the marginal efficiency of capital in the general theory depends on the relation between the replacement cost [the supply price of a capital asset] and its prospective yield. It is worth noting that the marginal efficiency of capital is still subject to the subjective swings of mood of the borrower).

However, the scale of investment is not always promoted by a low rate of interest as assumed in the general theory. Despite the availability of sufficient funds, screening and monitoring activities by (functional) lenders and investors still matter in order to respond to the general uncertainty from which lenders suffer, and thereby contribute to the optimal allocation of risk funds. For the banks as financial intermediaries, their nominal net profit from lending (particularly the 'floating rate' lending) is not affected by the change in the market reference rate (the funding rate for the banks), so far as the spread margin as risk premium towards the borrowers remains unchanged and the loan exposure remains the same. In other words, banks' net profit from the floating rate lending is affected only if (1) the banks consider the borrowers' lowered funding cost to reasonably lower their probability of default (to increase their probability of success), then the banks are willing to increase the loan exposure towards the borrowers when higher risk-adjusted returns are expected, and (2) the borrowers increase the demand of fund-raising for their investment. The above (1) is related to the banks' *subjective* judgment of screening and monitoring, while the above (2) depends on the borrowers' *subjective* sentiment of investment.

Second, we should ask how a low rate of interest can attract the ultimate fund providers. In the Marxian tradition, the analysis of banking credit and interest is undertaken on the basis of Marx's approach such that *stagnant* (or idle) money is systematically generated in the course of industrial accumulation, transformed into interest-bearing capital by the credit system and returned to accumulation to receive a share of surplus value (Itoh & Lapavitsas, 1999: 61). The money capital accumulated through the sale of commodity capital as well as the hoard of temporarily idle money of the industrial and commercial capitalists, workers, the state or anyone else are collected and centralized in the financial institutions, and transformed into potential money capital available to industrial capital (Fine & Saad-Filho, 2004). Needless to say, a lower (or zero) rate of interest would be less attractive to the idle money holders. Less money capital available to industrial capital would be less contributing to the capital accumulation for the society.

In the Marxian tradition, the differences between industrial capital and interest-bearing capital (IBC) are illustrated by respective circuits; it is widely known that industrial capital is expressed by M [money capital] - C [commodity inputs] - M' [money capital plus surplus value] for which money intervenes in the processes of production and exchange. In contrast, IBC is represented by M - M', where money stands apart from these processes (Marx 1981; Fine & Saad-Filho, 2004). In the conventional credit relationship between lender and borrower, the former realises the interest and the latter the profit of enterprise that remains, after the payment of interest, from the surplus value produced through the use of the borrowed money capital. It is worth noting that Marx emphasized that the price of the interest rate is 'irrational', since it bears no relation to any underlying production conditions. It depends on the competitive relations governing the classes of borrowers and lenders (Fine & Saad-Filho, 2004: 142-3). In the same token, Keynes argues that the rate of interest is not a reflection of return to savings (or price for sacrificing future consumption); rather it is a reward to savers for losing control over liquidity at present. In this sense, the liquidity preference of savers should have an important bearing in determining the actual rate of interest assuming capital is not scarce.

Like Marx, Keynes argues that capital is not as productive as labor. Thus, he acclaims entrepreneurs as well as efforts of labor and discourages the role of absentee owner because their income requires no genuine sacrifice. Keynes further views that the inequality of income that results from enterprise is desirable. However, inequality of income that results from ownership of wealth (the income of rentiers) is undesirable (Minsky, 1975). Both Marx and Keynes are very optimistic that the phase of capitalism will be over because For Marx, capitalism produces its own gravediggers (labor unrest and the resulting revolution) and for Keynes, capitalism is a transitional phase which will disappear when it accomplishes its work. Surprisingly enough, the phase is not over yet; but rather the influence of renters in the modern times is far greater than ever before. If so, how can we really squeeze the influence of functionless financiers on economy? Can an economy be money-free?

The question is not about the money itself but about the role money has been entrusted to play. Lapavistas (2003b: 50) rightly mentions what the neoclassical economists forget, ‘money buys goods but is never sold’. Treating money as commodity means particular goods is buying good which is absurd. But the neoclassical economists assume that at equilibrium prices, agents have no trouble in realizing sale or purchase of commodities because all goods, according to this school, are liquid. Consumers can finance their purchases of goods indifferently with money or with the supply of labor or of other goods. If so, money is distinct from other goods in name but not in function. Therefore, the world is frictionless virtual barter. In contrast, Marxian tradition views that money is not a substitute of goods or commodity. It is misleading to assume that the widespread commodity exchange could take place under barter conditions (Lapavitsas, 2003a). Lapavitsas (2003a) further argues that there is no evidence that a durable system of entirely money-free commodity transactions has ever existed. Basically money has broader social functions in a capitalist society, most clearly seen in relation to power and hierarchy. Money affords social power, since it can impel others to comply with its owner's will, for example, by placating opponents, mobilizing supporters, or hiring professional expertise (Lapavitsas 2003a: 60).

Keynes however, advocates for direct taxation on rentiers to bridge the income gap by reducing the influence of functionless investors-

> we might aim in practice (there being nothing in this which is unattainable) at an increase in the volume of capital until it ceases to be scarce, so that the functionless investor will no longer receive a bonus; and at a scheme of direct taxation which allows the intelligence and determination and executive skill of the financier, the entrepreneur *et hoc genus omne* (who are certainly so fond of their craft that their labor could be obtained much cheaper than at present), to be harnessed to the service of the community on reasonable terms of reward" (Keynes,1936: 345).

Keynes repeatedly emphasizes on the role of uncertainty as an influencing factor of interest rate. For Keynes interest rate is simply ‘… the reward for running the risk of uncertainty of one kind or another’. However under the recent trend of ugly neologisms –‘*marketization plus financialization*’ (Dore, 2000; Dore, 2011), the orthodox, traditional conceptualization of the decision-making process under ‘measurable’ uncertainty or risk has gained a total domination of the subject. The Post-Keynesian and heterodox view on the decision-making under 'unmeasurable' uncertainty *a la* Knight is nearly dead particularly among the practitioners in financial markets. Frank Knight drew a famous distinction between 'measurable uncertainty'or'risk', which may be represented by numerical probabilities and 'unmeasurable uncertainty' which cannot (Knight, 1921; Suzuki, 2011).

Since the consequences of actions extend into the future, accurate forecasting is essential for making objectively rational choices. But in the real world, most choices take place under conditions of *uncertainty*. The screening and monitoring actors (the banks as lenders and the investors as fund-providers) are working under conditions of uncertainty and bounded rationality. This means that monitoring activities are not mechanical, and that they are intrinsically based on subjective judgments that are often extremely difficult. The fundamental implication of Keynes' uncertainty is that all economically meaningful behavior derives from agents' efforts to protect themselves from uncertainty (Dymski, 1993). Uncertainty is fairly understated in academic arguments on the monitoring activities by the monitoring actors. While the functional financiers who challenge to deal with various ranges of credit risk under conditions of uncertainty are required for our society, it makes sense of the emergence of the function-less financiers who pay their efforts to protect themselves from uncertainty. The difficulty or inability of responding to the intensified uncertainty must be one of root causes of the trend of financialization.

From the Marxian political-economy perspective, capital is considered as the sum total of social relations between capitalists and workers, but also the ceaseless movement of value in pursuit of self-expansion. 'The latter is best thought of as a circular flow; capital value starts as money, becomes material inputs for production through market purchases (means of production and labor power), turns into finished commodities through production, and returns to money (augmented by surplus value generated in production, i.e. profit) through sale of finished commodities" (Lapavitsas, 2003a: 67). In the trend of financialization, interest-bearing capital (IBC) as represented by M - M' circuit where money stands apart from the production process, is also considered as the ceaseless movement of value in pursuit of self-expansion. On the other hand, IBC represents a claim on surplus value that has yet to be produced. In this light, since there can be no guarantee of production and appropriation of surplus value, it is hardly surprising that the financial sector should be capable of financing overproduction and generating spectacular speculative bubbles and equally spectacular crashes. And nor is it surprising that the possibility of fraud is ever present, even though 'fictitious capital' of this kind has become increasingly necessary for real accumulation (Fine & Saad-Filho, 2004).

If this Marxian view is held, it seems infeasible to eliminate the role of functionless financiers in the movement, while maintaining appropriate incentives to the 'functional' financiers. Or on other words, we cannot tame the spirit of financialization down without simply killing 'the golden goose'-the rentier; and at the same time, continuous financialization is engulfing the real economy. Perhaps, this dilemma can rationalize the partnership strategy upon the profit-loss sharing (PLS) between industrial capitalists and money capitalists (fund providers) widely observed in Islamic finance.

4. Compatibility of Islamic Principles of with Heterodox Thinking

The Marxian view on IBC and merchant's capital is suggestive of understanding the Islamic prohibition of *Riba*. Islam, a religion born in the Arabian Desert, where trade constituted the most important, 'perhaps even the sole economic activity, favors merchants, property rights, free trade and market economy' (Çizakça, 2011: xv). In this context, Islam is called the religion for merchants (Ayub, 2007; Çizakça, 2011). The business ethics in the Islamic mode of transactions are related to the civilized urban way of life at the birth of Islam. The holy Prophet had spent half of his life working as a merchant in Mecca, where the urban culture was flourished and the values for facilitating fair transactions among the merchants in equal positions were shared. The holy Prophet mentioned that trade constituted nine-tenth of the livelihood of early Muslims. In fact, of the four righteous Caliphs, Abu Bakr was a cloth merchant and Uthman was an importer of cereals (Çizakça, 2011: xiv).

The values being shared among merchants have developed the concept of contracting and the importance of respecting mutual property rights in the Islam community. Islam recognizes the role of market and the freedom of individuals in business and trade while restraining the freedom to engage in business and financial transactions on the basis of a number of prohibitions, ethics and norms. It is widely known that the prohibition of *Riba*, *Gharar* and *Maisir* (gambling) is the most strategic factor that defines invalid and voidable contracts and demarcates the overall limits which should not be crossed (Ayub, 2007: 12).

Interest constitutes the major portion of rentiers income and is considered a core element of financialization. An examination of world's dominant religions shows that they all prohibited interest as far as history is concerned. The Abrahamic faith traditions - Judaism, Christianity and Islam - took initial strides to prevent adherents from charging any interest on loans (Looft, 2014). While Jewish and Christian have both evolved to draw distinctions between acceptable interest and usury, Islam still explicitly forbids charging any interest on loans. Usury is referred to as a rate of interest greater than that which the law or public opinion permits (Looft 2014). Looft (2014) points out that nevertheless, there are still voices within Christian communities that deride all forms of interest as usury, referring to the following poem written by Peter Maurin who co-founded the Catholic Worker Movement in 1933; '1. Before John Calvin people were not allowed to lend money at interest. 2. John Calvin decided to legalize money-lending at interest in spite of the teachings of the Prophets of Israel and the Fathers of the Church. 3. Protestant countries tried to keep up with John Calvin and money-lending at interest became the general practice. 4. And money ceases to be a means of exchange and began to be a means to make money. 5. So people lent money on time and started to think of time in terms of money and said to each other: "Time is money"'(Looft, 2014: 114-5).

While the heterodox perspective is still not sure if the rate of interest should be lower and ultimately zero, Islam completely prohibits it. Islam has not relented to pressures from the marketplace and has continued to maintain its stance that charging interest on loans is usurious and a violation of Islamic law. As Looft (2014) points out, the logic behind this is that lending money at interest without any means of sharing risk between lender and borrower creates a relationship where weak and vulnerable individuals can be easily exploited by more powerful ones. However, the prohibition of *riba* makes it difficult to collect and centralize the temporarily idle money in order to transform into potential money capital available to industrial capital. The prohibition of *riba* on the one hand and the difficulty of collecting deposit without offering interest on the other result the rise of Islamic banking dominated by *Shari'ah*-compliant asset-based financing including *murabaha* (mark-up contract), *bai-muajjal* (variant of *murabaha*), *bai-salam* (forward sale contract), and *ijara* (leasing) rather than by the dominance of profit and loss sharing *mudaraba* (trust based contract) and *musharaka* (partnership/equity based contract) that are developed by following the divine rules prescribed in Islamic *Shari'ah* (Çizakça, 2011). The current profit-loss sharing risk provides an idea of the difficulty in assuming the equity-based financing with higher credit risk in practice. As Suzuki & Uddin (2014) point out, it is impractical to expect the acceleration of the participatory financing without preserving much higher bank rent for Islamic banks for covering further *Shari'ah* profit and loss sharing risk. The Islamic logic and ethics are compatible with the Marxian political-economy view on money and credit to a great extent.

Avoiding *Gharar* is another salient principle of Islamic finance. In the Islamic mode of investment and financial intermediation, excessive uncertaintyis perceived in two dimensions: one refers to lack of clarity in the terms and essence of the contract, the other refers to the uncertainty in the object of the contract (Ayub, 2007; El-Gamal, 2006). Complete contracting is intrinsically impossible. Therefore, some measure of uncertainty is always present in contracts. El-Gamal (2006: 58) notes 'jurists distinguished between major or excessive *Gharar*, which invalidates contracts, and minor *Gharar*, which is tolerated as a necessary evil'. Also, the uncertainty in the object of the contract cannot be avoided in any business. 'The problem, however, was that the extent of uncertainty making any transaction *Haram* had not been clearly defined (Ayub, 2007: 58). Ayub (2007) refers to *Gharar-e-Kathir* and *GhararQalil* (too much and nominal uncertainty) and agrees that only those transactions that involve too much or excessive uncertainty in respect of the subject matter should be prohibited. Saati (2003) suggests that the *Hadith* (which prohibits *gharar*) does not intend to prohibit all *gharar*, but intends to prohibit *gharar*which can cause dispute and cannot be tolerated.

Basically, Islamic principles of economics focus on clarity and lack of ambiguity, just and fair treatment or all and care for the rights of others (Ayub, 2007). So far as these principles are necessarily ethical, incubating small and middle-sized enterprises (SEMs)would be acceptable to an extent in which the associated major uncertainty can be shared and absorbed in the community through an adequate profit-loss sharing agreement (Suzuki, 2013). Ayub (n.d: 2) mentions 'for a more efficient economy, we must promote systems in which people work in productive pursuits rather than unproductive ones. Change the system to relate it with real sector activities and all those clever dealers who earn huge profits out of thin air could become doctors, industrialists, business people and teachers instead'. This provides with the evidence that engagement in enterprise rather than speculation seems to be preferably considered in the Islamic mode of investment. The prohibition of *Gharar* in speculation is considered as the wisdom for minimizing the potential periodic financial disaster. In parallel, under the prohibition of *Gharar* (also the profit-loss sharing) framework, it may have created a dilemma of the so-called '*Murabaha* syndrome' leading to the financial disintermediation (particularly the dry-up of long-term funds) in the potentials SMEs. Long-term growth may suffer as a result. Based on the best effort to avoid the incompleteness of contract, it might be acceptable, to an extent in which the associated major uncertainty in *enterprise* can be shared and absorbed in the community through an adequate profit-loss sharing agreement, to incubate small and micro-enterprises in agricultural and industrial sectors (Suzuki, 2013). How Islamic financial institutions will tackle the *Murabaha* syndrome while improving the financial intermediation to industrial potentials should be further argued.

In parallel, it is worth arguing that the wisdom in the prohibition of *Gharar* can possibly squeeze function-less financiers in the financial derivatives and hedge-products market. In this context we find Marx's *labor theory of value* very sympathetic. Prohibition of *riba* and indirectly prohibition of *gharar* in the Islamic mode would to some extent restrain the rate of exploitation. Probably, the rate of profit in the Islamic mode would be accordingly restrained. The circulation of M-C-M' or M-M' in the Islamic mode is considered slower than that in the capitalist mode. On the one hand, the Islamic principles are contributing to squeezing the 'function-less' financiers by not giving them the opportunity of exploiting. On the other hand, the Islamic principles are less contributing to incubating the 'functional' financiers who have the partner's strategy in the participatory financing for incubating new industries.

Islamic banks mobilize deposits on the basis of profit-and-loss sharing agreement and to some extent on the basis of *Wakalah*against pre-agreed service charges or agency fees. While sharing profit or loss arising on investments, they earn a return on their trading and leasing activities by dint of the risk and liability undertaken and adding value in real business activities (Ayub, 2007). On the other hand, the following threat and sanctions mechanisms encourage prudent screening and monitoring. First, *Shari'ah*rules are the cornerstone of Islamic financial products and services. If depositors or customers become aware that the products they have in their portfolios are not *Shari'ah*-compliant, it would seriously undermine customer confidence in the Islamic bank concerned or, on a larger scale, in the Islamic financial services industry as a whole (Bhambra, 2007: 204-5). Second, a prudent or conservative credit screening policy is required to reduce the probability of loss, particularly in the case of *mudaraba*- or *musharaka*-based financing. Third, risk-averse depositors will look for low-risk forms of financing, for instance, *murabaha* and other similar asset-backed financing. In this context, El-Gamal (2006) refers to what Islamic finance practitioners call 'displaced commercial risk'. This may arise if Islamic bank depositors suffer a loss compared with conventional bank depositors and therefore, withdraw their funds from the Islamic bank (El-Gamal, 2006:155). Fourth, strict practice of profit-and-loss sharing principle is a rarity in Islamic banking operations and in most cases the return for the depositors is homogenous for all banks irrespective of their scales of profitability (Chong & Liu, 2009; Farook & Farooq, 2011, Zaher & Hasan, 2001). It is highly likely that some Islamic banks are hesitant to share losses with their depositors maintaining their franchise value as prudent monitors to avoid the displaced commercial risk. Credit risk is similar to conventional banking, but credit risk management and recovery process are far more complicated in the Islamic banking system than in conventional banking (El Tiby, 2011). Unlike conventional banks, Islamic banks have to absorb not only the credit risk but also the risk associated with the compliance of

Islamic *Shari'ah*, that is, *Shari'ah* risk. Accordingly, in addition to the difference between the rates of profit received and profit paid (borrowing rate and lending rate respectively in conventional banking), Islamic banks need an extra cushion to absorb the unexpected loss and the transaction costs associated with the *Shari'ah* compliance to maintain the franchise value.

5. Concluding comments

We have attempted, in this paper, to link three prominent issues relevant to the financial world today – the causes and consequences of financialization, the heterodox perspective on the concerned issues and the compatibility of heterodox school to Islamic prohibition of *Riba* and *Gharar*. Following financial liberalization, the world economy relied too much on financing activities leaving the real economy behind. This trend has paved the way for innovation of new financial products and instruments enticing increased number of players to capitalize on these instruments. At its peak, financing activities expanded to such an astronomical level that the real economy could not afford to sustain it. The eventual burst of bubble left the world into complete disarray resulting decline in consumer wealth estimated to be trillions of dollars accompanied by prolonged unemployment. We have argued that financialization facilitated the emergence of a new capitalist class that has been able to influence and capitalize on monetary policy particularly the interest rate. Moreover, the tendency to transform fundamental uncertainty into risk through technological innovation has enabled firms to gamble without limit. These two elements we have examined shedding analytical lights on the heterodox school.

In spite of their enormous importance for contemporary capitalism, Marxian studies of money and finance have progressed relatively slowly, with little generally being said about the more fundamental issues of the nature of finance and the relationship between financial and industrial capital. Many of the questions Marx asked seem surprisingly suggestive of transcending the trend of financialization. Particularly his concept on the role of money is an essential element to be considered in determining the level of financial activities in relation to real economy. Moreover, Keynes' discussion on fundamental uncertainty is closely associated with the function of money. We have argued drawing on Marxian and the economics of Keynes that money is the cornerstone of all social endeavors as opposed to an elemental state of barter viewed by the neoclassical school.

These two elements – interest and uncertainty- are the core principles of Islamic finance. Though Keynes' ideology is not certain if the interest rate can be zero, Islam is outspoken about zero rate of interest. It prohibits all sorts of *riba*and*gharar* and encourages profit-and-loss sharing based financial contract instead. It is unfair in the view of Islam that the capitalist class would enjoy guaranteed return while the entrepreneurs suffer from fundamental uncertainty associated with futures. It is the uncertainty for which Keynes argues for positive interest rate. However, the existence of uncertainty on the one hand and the non-existence of interest on the other make it difficult for Islamic financial institutions to mobilize deposits and expand loans. This has resulted the concentration of Islamic *Murabaha*financing instead of true profit and loss sharing contract. An extended explanation on the so-called *Murabaha* syndrome and its possible solutions are the issues we keep for our future discussion.

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