




ANALYZING THE PRACTICE OF *MUSHĀRAKA MUTANĀQISA* IN THE ISLAMIC BANKING INDUSTRY: THE KINGDOM OF BAHRAIN AS A CASE STUDY



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ABSTRACT

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One of the modes of Islamic financing includes a *mushāraka* (partnership) mode. *Mushāraka mutanāqisa* (diminishing partnership) is considered to be one of the forms of *mushāraka*. As the purpose and end result of this product seems to be considerably similar to that of other Islamic financial products, this research empirically analyzes whether, when, and why Islamic banks may opt for a *mushāraka mutanāqisa*. Although the Kingdom of Bahrain may arguably be considered as one of the global Islamic financial hubs, there seems to be limited empirical researches investigating the practice of *mushāraka mutanāqisa* by using the Kingdom of Bahrain as a case study. By using a qualitative methodology, this research empirically investigates the practice of *mushāraka mutanāqisa* by four Islamic banks (consisting of two for each Islamic retail and Islamic wholesale banks). The results suggest that perhaps due to various reasons and risks involved, the utilization of *mushāraka mutanāqisa* may relatively be noticeably lower than other Islamic financing products. Additionally, there seems to be no indications that the utilization of *mushāraka mutanāqisa* may increase in the near future. This research may have contributed to knowledge by adding to literature contemporary empirical data pertaining to the practice of *mushāraka mutanāqisa* in the Islamic banking industry in the Kingdom of Bahrain.

Contribution/ Originality: This research may be one of the few contemporary studies that use the Kingdom of Bahrain as a case study to empirically analyze the practice of *mushāraka mutanāqisa* in the Islamic banking industry.

1. INTRODUCTION

Modern Islamic finance may have started out as a small project in 1963 (Hassan *et al.*, 2012). As of 2017, the total assets of the Islamic financial industry have been estimated to reach around USD 2.05 trillion (IFSB, 2018). Generally, it may be considered that Islamic finance uses several modes of financing mechanisms, including sale, lease, or partnerships (Ayub, 2007). These modes of financings may have differentiated Islamic finance from conventional finance (Abdul-Rahman, 2010). However, a number of authors have argued that these distinguishable modes of financings may in reality be similar or equivalent to conventional methods of financings (El-Gamal, 2006). For example, rather than providing an interest-based loan, a *murābaha* (cost-plus sale) involves an Islamic bank purchasing an asset and selling it to a customer on a deferred basis (Kettel, 2011). This has been argued to be an interest-based loan through a disguise; rather than directly providing liquidity to a customer and charging interest, an Islamic bank may finance an equal amount and sell it on a deferred basis by adding a profit margin equivalent to

an interest rate (El-Gamal, 2006). In one form or another, the same argument may be applied to many other Islamic financial products.

One of the Islamic financing tools falls under the realm of a partnership mode, known as a *mushāraka* (Abdul-Raheem, 2013). Several types of *mushāraka* products exist, including what may commonly be known as a *mushāraka mutanāqisa* (diminishing partnership) (Moriguchi *et al.*, 2016). In a *mushāraka mutanāqisa*, an Islamic bank may finance a client by partially owning the purchased asset, whereby the client gradually purchases the shares of the Islamic bank through periodic payments and ultimately leading to a full ownership by solely the client (Sori *et al.*, 2017). However, the end-result of this product seems similar to other Islamic financings products, such as a *murābaha* or an *ijāra muntahia bil tamlik* (lease-to-own), where both products consist of deferred profit-based methods of financings where a client ultimately attains ownership of the financed asset (Hassan *et al.*, 2012).

To this end, we pose the following questions: when and why would an Islamic bank prefer to choose a *mushāraka mutanāqisa* product instead of any other Islamic financial product? What are the differences, distinguishing features, advantages or otherwise, that may result an Islamic bank to specifically opt for this Islamic financing product? What is the practice with regards to *mushāraka mutanāqisa* in the Islamic banking industry? An empirical enquiry into answering such questions may be beneficial from a knowledge standpoint. In addition, although the Kingdom of Bahrain has been arguably considered as one of the Islamic financial hubs (Hidayat and Al-Khalifa, 2018), it nevertheless seems that limited Islamic finance empirical researches exist by using this jurisdiction as a case study. A review of literature suggests that this may even be truer in the case of empirically investigating the practice of *mushāraka mutanāqisa* in the Kingdom of Bahrain. Thus, we try to fill this research gap through our empirical enquiry, as contemporary empirical results pertaining to *mushāraka mutanāqisa* practices by the Islamic banking industry in the Kingdom of Bahrain may be a valuable contribution to knowledge. Thus, the following aims were developed for this research:

- Analyze the theories and phenomena underlying a *mushāraka mutanāqisa*, including the Shari'a ruling for *mushāraka mutanāqisa*.
- Investigate the practice, and understand when and why Islamic banks opt for a *mushāraka mutanāqisa* as an Islamic financing tool, by using the Kingdom of Bahrain as a case study.

Following the introduction, section 2 succinctly reviews literature pertaining to *mushāraka*, *sharikat al-'inan*, and *mushāraka mutanāqisa*. It thereafter reviews literature pertaining to the Shari'a ruling of *mushāraka mutanāqisa*. Section 3 is the research methodology section that explains the use of a qualitative methodology, and the Kingdom of Bahrain as a case study. Section 4 provides the empirical data and analysis, while section 5 offers a conclusion.

2. REVIEW OF LITERATURE

2.1. *Mushāraka* (Partnership)

The etymological meaning of *mushāraka* (sometimes referred to as *sharika* in classical Shari'a literature) may be referred to as sharing (Ibn Mandhur, 2013). Literature tends to suggest that the idiomatic meaning of *mushāraka* according to the *fuqahā* (Shari'a jurists) is similar to that of its linguistic meaning (Ibn Rushd, 1998). In modern terms, *mushāraka* has been defined as a contractual agreement between two or more parties, where the parties combine their assets, labour, or liabilities for the purpose of generating profits (AAOIFI, 2015; Ali and Hussain, 2017). In one form or another, profits and losses in a *mushāraka* are shared according to predetermined ratios (Rammal, 2004). Some authors have explicitly clarified that solely the profits are distributed in accordance to predetermined ratios while the losses are shared in accordance with the financial contributions made by each partner (Usmani, 2002).

Fiqhi (Islamic jurisprudential) literature tends to suggest that there are many segments of *mushāraka* (Shabir, 2007). This includes *sharikat al-'inan* (contractual partnership), *sharikat al-wujuh* or *al-thimam* (liability partnership), and *sharikat al-a'mal* (vocational partnerships or partnerships for undertaking difficult work or accepting jobs)

(Mash'ur, 1990). In the following section, we focus on the definition of one type of these partnership segments, which is *sharikat al-'inan*. This is because literature suggests that *mushāraka mutanāqisa* originated from the segment of *sharikat al-'inan* (AAOIFI, 2015), and while this research pertains to the concept and practice of *mushāraka mutanāqisa*.

2.1.1 Sharikat Al-'Inan (Contractual Partnership)

The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) has defined *sharikat al-'inan* as a partnership between two or more parties 'whereby each partner contributes a specific amount of money in a manner that gives each one a right to deal in the assets of the partnership, on condition that the profit is distributed according to the partnership agreement and that all the losses are borne in accordance with the contribution of each partner to the capital' (AAOIFI, 2015). Classical *fiqhi* literature seems to also indicate that definitions relating to *sharikat al-'inan* are similar to that of AAOIFI (For example, please see: Ibn Qudamah (1997)). In addition, the definition provided by AAOIFI may support the notion that although profits are distributed according to a predetermined agreement, losses are solely borne in accordance with the contributions of each partner. It also seems that that this definition may also be viewed as similar to a normal *mushāraka*.

As indicated earlier, *sharikat al-'inān* is the segment of a *mushāraka* that is claimed to have given birth to one of the contemporary Islamic financial forms of *mushāraka*, namely *mushāraka mutanāqisa*. As the research particularly relates to the practice of *mushāraka mutanāqisa* as an Islamic banking product, the following section reviews literature pertaining to *mushāraka mutanāqisa*.

2.2. Mushāraka Mutanāqisa (Diminishing Partnership)

Interestingly, a review of literature indicates that the terminologies relating to the concept of *mushāraka mutanāqisa* are expressed in various forms. For example, *mushāraka mutanāqisa* is also sometimes referred to as *mushāraka muntahia bil tamlik* or *mudhāraba muntahia bil tamlik* (Al-Enezi, 2015). The terminology '*muntahia bil tamlik*' refers to when one party is expected to ultimately own the commodity/asset (Al-Hafi, 2000). Such a terminology may most commonly be associated with the *ijāra* product, known as *ijāra muntahia bil tamlik* (for example, please see: (Ayub, 2007). This in itself may indicate that similarities may exist between diverse types of Islamic financial products.

On a separate note, *mushāraka mutanāqisa* has been defined in literature a financing tool where the share of an Islamic bank in a designated property (in a joint ownership) gradually decreases through a continuing sale of its shares to a customer, whereby installments paid by the customer (as a partner) represent purchasing certain shares off the Islamic bank (Hassan *et al.*, 2012). Following the completion of the financing tenor, the customer as a partner would have purchased off all the shares owned by the Islamic bank, ultimately leading to the customer owning the underlying property in full. Literature tends to suggest that this financing tool has been one of the contemporary innovations innovated by modern Islamic banks (Al-Enezi, 2015).

A *mushāraka mutanāqisa* generally involves combining more than one contract into this financing mechanism, such as partnership and sale (Al-Enezi, 2015). Or, it may combine more than two contracts, such as partnership, sale, and lease (Al-Shubaili, 2002). However, some literature pertaining to modern Islamic banking solely mentions that this product involves a chain of three contracts, without necessarily making mention of the ability to solely use two contracts (Hassan *et al.*, 2012). Literature further tends to indicate that this product has been a result of modern Islamic financial engineering (Al-Enezi, 2015).

To elaborate with regards to the three contracts involved in a *mushāraka mutanāqisa*, the first contract involves a joint ownership between an Islamic bank and the client, where the client promises to purchase the shares owned by the Islamic bank (Hassan *et al.*, 2012; Mikail, 2016). The second contract involves a lease agreement between an Islamic bank and client under the joint ownership, whereby units of shares are transferred to the client under the

lease agreement (Hassan *et al.*, 2012). Based on this earlier agreement, a third contract is then entered into where the client gradually purchases off the shares of an Islamic bank (Hassan *et al.*, 2012). Thus, the reason why this type of *mushāraka* is referred to as *mutanāqisa* (diminishing) is because the joint partnership gradually diminishes where the client ultimately attains full ownership of the underlying property (Nor *et al.*, 2019). To clarify, the method in which the Islamic bank obtains a profit is by selling its shares (on a gradual basis) to the client with a mark up profit rather than its initial price (Asadov and Ibrahim, 2018).

Based on the literature provided in this section, Figure 1 below illustratively displays a visualization of how a *mushāraka mutanāqisa* transaction may possibly look like:

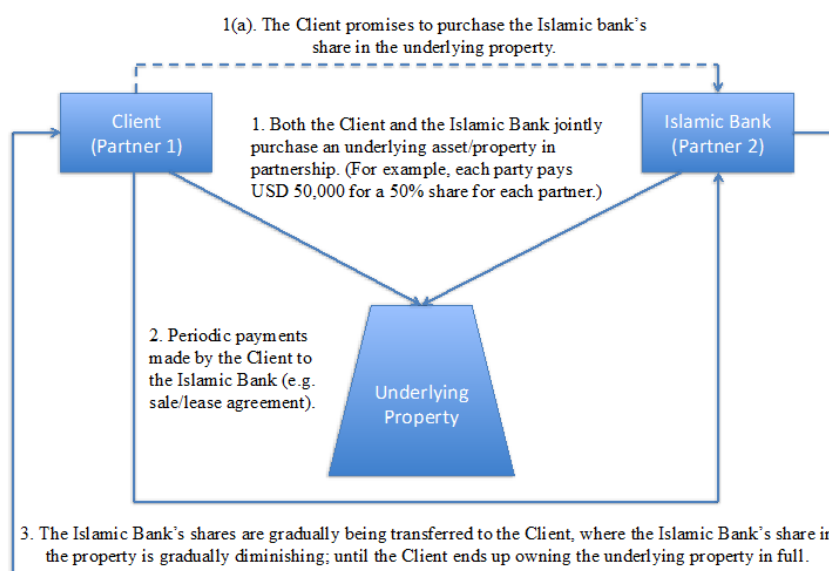


Figure-1. Visualization of *Mushāraka Mutanāqisa*.

Since this financing tool is considered to be the prime focus of the research, the following section reviews literature in relation to the Shari'a ruling of *mushāraka mutanāqisa*.

2.2.1 Shari'a Ruling for *Mushāraka Mutanāqisa* (Diminishing Partnership)

There seems to be a discrepancy in literature relating to the Shari'a ruling of *mushāraka mutanāqisa*. On one hand, some literatures indicate that Shari'a jurists unanimously agree on the permissibility of *mushāraka mutanāqisa*. For example, in regards to *mushāraka mutanāqisa*, a respected author mentions: "The jurists are unanimous on the permissibility of this arrangement" (Ayub, 2007). On the other hand, other literatures indicate that there is a difference of opinions amongst Shari'a jurists regarding the permissibility of *mushāraka mutanāqisa* (Al-Enezi, 2015). This may be due to the difference in publication dates of the mentioned literature, since contemporary Shari'a rulings may be modified in accordance with the time, place, and/or practice. Nevertheless, it seems that although there may be a minority of Shari'a jurists, who view a *mushāraka mutanāqisa* as being prohibited in Shari'a, evidence indicates that there may be a sizeable majority who view this product as being Shari'a compliant. This claim may further be backed by evidence since AAOIFI deems this product as permissible (while setting out the necessary controls to implement this product in accordance with the Shari'a) (AAOIFI, 2015). As such, Islamic banks may opt for this Islamic financing tool if they view it as being the most suitable product to finance their clients under certain circumstances.

2.3. Deliberation on Literature

A *mushāraka mutanāqisa* may represent an Islamic financing tool where an Islamic bank finances its client through partial ownership, thereafter selling its shares to the partnering client at a higher price. The profit obtained

through the marked up selling price may consist of a valid sale following the legal ownership of an underlying asset by an Islamic bank (Rahman *et al.*, 2018). Thus, this financing mechanism and profit may be permissible according to Shari'a, and may represent one of the Islamic financing techniques that avoid the engagement in interest-based activities (which is prohibited in Shari'a) (Abdul-Rahman, 2010). This may therefore be considered as one of the valid substitutes to conventional financings. However, why would an Islamic bank specifically opt for a *mushāraka mutanāqisa* product rather than any other Islamic financial product? Are not other Islamic financial products (such as a *mudhāraba*, *ijāra*, or a *murābaha*) considered as suitable substitutes?

We further contemplate on the possible purpose and end result of a *mushāraka mutanāqisa*. Through certain procedural requirements, an Islamic bank would finance a client with a specific amount for a financed asset, while intending to thereafter retrieve its financed amount with an additional profit (Effendi and Pratiwi, 2017). Ultimately (following the completion of the financing period), the client ends up owning the property in full. It may be asked however, is this not the same as many other Islamic financing products? For example, is not the purpose and end result of a *murābaha* to finance a client with a specific amount, while intending to thereafter retrieve its financing amount with an additional profit? In addition, in one form or another, does the client not ultimately own the financed asset? To present another example, is not the purpose and end result of an *ijāra muntahia bil tamlik* similar to the example provided for a *murābaha*? Why specifically opt for a *mushāraka mutanāqisa* and furthermore, why was this product innovated by Islamic banks? The review of literature tends to suggest that *mushāraka mutanāqisa* has distinguishing features relative to other Islamic financing tools. For example, rather than initially fully owning an asset and leasing it to a client through an *ijāra* contract, a *mushāraka mutanāqisa* involves partnering with the client by jointly owning an asset prior to gradually selling its shares to a client. Another example, rather than immediately selling an underlying asset to a client through a deferred sale and/or *murābaha* (thereby transferring the title deed to the client immediately upon signing the financing contract), a *mushāraka mutanāqisa* involves an Islamic bank to firstly and partially own an underlying asset prior to selling its shares to a client. This in itself may reveal some distinguishing features of a *mushāraka mutanāqisa* relative to other Islamic financial products. From the outset, these differences seem to mainly relate to the timing of transferring the legal ownership of an underlying property. However, why would the timing of transferring legal ownership be a matter of significance? First, as there may probably be certain risks associated with either owning an asset or the lack of ownership (Mostafa *et al.*, 2016; Subky *et al.*, 2017) a *mushāraka mutanāqisa* may represent a mechanism to mitigate those risks associated with either owning an asset in full or the lack of ownership (Nor *et al.*, 2017). It seems through an initial (joint) partial ownership, an Islamic bank may be able to mitigate those risks to avoid the risks involved as a result of full ownership or lack of ownership. Thus, one conclusion may be that a *mushāraka mutanāqisa* may be used following a risk assessment of certain transactions (Asadov *et al.*, 2018). To further deliberate, why would an Islamic bank want to either own an asset or disassociate itself from ownership? Literature tends to suggest that an Islamic bank may want to fully own an asset to address credit risks in the case of a default. In contrast, Islamic banks may want to disassociate themselves from owning an asset to avoid some mandatory costs/expenses resulting from ownership. Thus, under certain circumstances, it seems that a *mushāraka mutanāqisa* may somewhat represent a middle ground for mitigating these two types of risks.

As the above represents an analysis resulting from literature, section four empirically analyzes the practice of *mushāraka mutanāqisa*, to possibly understand whether, when, and why Islamic banks opt or execute *mushāraka mutanāqisa* transactions.

3. RESEARCH METHODOLOGY

This research uses a qualitative methodology, and uses the Kingdom of Bahrain as a case study. A qualitative methodology may be an effective methodological approach when theorizing prominent issues (Corbin and Strauss, 2008). Furthermore, as mentioned in the introduction section, the Kingdom of Bahrain has arguably been

considered as one the global Islamic financial hubs (Hidayat and Al-Khalifa, 2018). Nevertheless, it seems that there may be limited contemporary Islamic finance empirical researches using the Kingdom of Bahrain as the jurisdiction for a case study. Thus, the empirical section attempts to partially fill this research gap by adding to literature contemporary empirical data relating to *mushāraka mutanāqisa* practices by Islamic banks in the Kingdom of Bahrain.

3.1. Methods of Data Collection and Analysis

Both primary and secondary data are used for the empirical enquiry. The primary data collection process involved interviews with internal Shari'a employees at Islamic banks in the Kingdom of Bahrain. This was a result of the expectation that not only would the internal Shari'a personnel be aware whether *mushāraka mutanāqisa* (diminishing partnership) transactions are utilized by their respective Islamic banks, but rather may also be aware of the reasons or rationales behind the choices of product utilization. Therefore, it was expected that these respected interviewees might be aware of why and when *mushāraka mutanāqisa* transactions were being utilized if it was adopted. In line with the research aims, and as a result of the review of literature section, the researcher simply asked the interviewees whether, why, and how Islamic banks utilize *mushāraka mutanāqisa* as an Islamic financing mechanism.

On the other hand, secondary data were reviewed in order to possibly validate the primary data information. We briefly review the latest available financial statement of each Islamic bank (as of 31 December 2018) to look for any indications whether the respective Islamic banks were utilizing *mushāraka mutanāqisa* as an Islamic financing tool. Therefore, the results of the secondary data were used in cross-examination with the primary data in order to possibly strengthen the authenticity of the data collection results. Additionally, this secondary was used in order to possibly attain information of the asset size of *mushāraka mutanāqisa* relative to other Islamic financing products. All data obtained were qualitatively analysed. As for the data coverage, the research covers the Islamic banking industry as a whole by selecting two Islamic retail banks and two Islamic wholesale banks as units of analysis. This was in order to possibly attain a more comprehensive insight into the practices of *mushāraka mutanāqisa* in the Islamic banking industry as a whole rather than solely focusing on one sector. Furthermore, the diversification of the units of analysis in terms of Islamic banking classification may be more informative and may be used for cross-comparison purposes. To respect their privacy, the research refers to these units of analysis as Islamic retail bank A, Islamic retail bank B, Islamic wholesale bank C, and Islamic wholesale bank D. Figure 2 below illustratively displays the case study design used for the empirical enquiry:

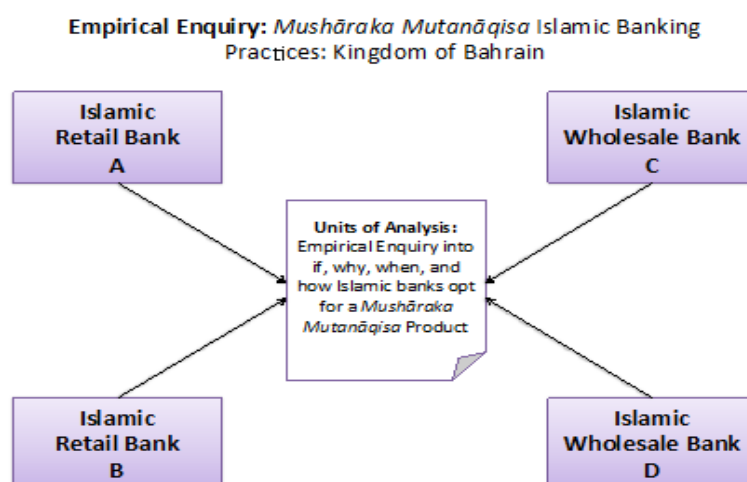


Figure-2. Research methodology: Case study design.

To conclude, the interviews conducted with the internal Shari'a personnel for Islamic retail bank A was on 11 January 2020, Islamic retail bank B on 12 January 2020, while was conducted for both Islamic wholesale banks C and D on 9 January 2020. The following section displays the empirical data and analysis for the empirical enquiry.

4. Empirical Data Analysis

4.1. Islamic Retail Bank A

4.1.1. Primary Data for Islamic Retail Bank A: Interviews

The primary data collection process for Islamic retail bank A suggested that Islamic retail bank A engages in *mushāraka mutanāqisa* transactions. The history behind the use of this Islamic financial product seems to be an interesting one. First, the use of *mushāraka mutanāqisa* by Islamic bank A started roughly around 1980-1990 (considered to be the early years of the establishment of Islamic bank A). Then, the product would solely be utilized if a client intended to purchase a property for business purposes, where the client intends to lease the financed property for income generating purposes. With regards to the practice, Islamic retail bank A would jointly purchase the property with the client as a partner, where the bank then leases its share to the client for a specified amount of time. Following the completion of the tenor, Islamic bank A would then sell its share to the client, and therefore the client would ultimately end up owning the property in full. This seems to support the review of literature section where it suggests that a *mushāraka mutanāqisa* consists of a chain of three contracts, namely: a partnership, lease, and sale.

However, the primary data collection process further revealed that the practice of using a chain of three contracts continued until around 2007. Following 2007, the practice of *mushāraka mutanāqisa* was altered. First, Islamic bank a started using the *mushāraka mutanāqisa* product whether a client sought the finance for personal or business purposes. Second, the practice of *mushāraka mutanāqisa* was changed into having solely two contracts rather than three, namely partnership and sale. Therefore, this seems to support the review of literature section that suggests that the practice of *mushāraka mutanāqisa* may consist of either two or three contracts. This argument may further be supported because starting from 2019, Islamic retail bank A went back to implementing *mushāraka mutanāqisa* the same way it did prior to 2007 (using a chain of three contracts: partnership, lease, and sale).

In this regard, an enquiry was made in relation to why the practice of *mushāraka mutanāqisa* changed the first and/or second time, and why/when would the *mushāraka mutanāqisa* product be viewed as the most suitable (for example: as opposed to any other Islamic financial product).

It may be imperative to note first that the respective interviewee indicated that the practice prior to 2007 was not clear in an apparent manner. Prior to 2007, it was not clear why Islamic retail bank A opted for a *mushāraka mutanāqisa* product in certain cases as opposed to other Islamic financial products. What may have been clear is that *mushāraka mutanāqisa* was introduced by the Shari'a Supervisory Board of Islamic retail bank A (for example: as a substitute to an interest based loan) during the early stages following the establishment of Islamic bank A. This may somewhat indicate that the practice of *mushāraka mutanāqisa* may not have necessarily started out due to it being viewed as the most suitable Islamic financial product (for example: as opposed to other Islamic financial products), but rather was one of the options Islamic banks started using as an alternative to interest based loans. This notion may be supported since Islamic retail bank A was one of the first Islamic banks to be established in the Kingdom of Bahrain, and thus the practice of modern Islamic banking may have been considered as fairly new at the time (1980-1990 period).

With regards to the practice, the primary data collection process further revealed that the use of three contracts for a *mushāraka mutanāqisa* (during the 1980-90 until 2007 period) seemed to also have been practiced as a result of Shari'a Supervisory Board resolutions. Since Islamic banking was relatively considered a new practice, it seems that the implementation of Islamic banking products may have been a result of Shari'a Supervisory Board

interpretations or guidance relating to *mushāraka mutanāqisa* (and perhaps other Islamic financial products), rather than a choice Islamic retail bank A would have between choosing one form of *mushāraka mutanāqisa* or another.

To support this argument, when an enquiry was made regarding why the practice of *mushāraka mutanāqisa* was altered specifically following 2007, the interviewee responses revealed that this was a decision by the Shari'a Supervisory Board. The Shari'a Supervisory Board of Islamic bank A expressed an opinion that *mushāraka mutanāqisa* was a viable product to be used for both personal and business purposes (as opposed to solely business purposes). To elaborate, the Shari'a Supervisory Board mentioned that Islamic retail bank A may jointly purchase a property with a client as a partner regardless of whether the client sought the finance for personal or business purposes, and further expressed that Islamic retail bank A may sell its shares gradually to the client through a sale contract without the need to have a lease agreement between the partnership and sale contract. This may thus suggest that the practice of *mushāraka mutanāqisa* (and perhaps other Islamic financial products) may not have necessarily been as a result of decisions solely by management or risk assessments, but may have rather had a reliance on Shari'a Supervisory Board resolutions.

As the analysis in this section tends to suggest that the utilization of *mushāraka mutanāqisa* may not have necessarily been as a result of solely risk assessments or other financial assessments, but rather implementing Islamic banking practices as guided by the Shari'a Supervisory Board, this may evidence that the practices of Shari'a Supervisory Boards may be that of an influential one. However, as it did not seem to be empirically clear why a *mushāraka mutanāqisa* was being utilized as a product as opposed to other Islamic financial products (for example: *ijāra muntahia bil tamlik*), an enquiry was thus made regarding this matter. In this regard, the primary data collection process may have revealed some distinguishing features of a *mushāraka mutanāqisa* that may serve as a justification for utilizing *mushāraka mutanāqisa* as opposed to other Islamic financial products (for example: *ijāra muntahia bil tamlik*). To possibly clarify this matter through an example, an *ijāra muntahia bil tamlik* represents a financing mechanism where an Islamic bank would fully own the underlying property and lease the property to a client. At the end of the lease period, the legal ownership of the property is transferred to the client. However, if a client approaches Islamic bank A, and seeks a finance of 40% of an underlying property (indicating that the client would contribute 60% of the purchasing price), it may not be feasible, or fair, from the perspective of the client for the Islamic bank to fully own the property. The client may prefer to (partially) own the underlying property as the client is contributing a significant amount of the purchasing price. It may be viewed as unfair from the perspective of the client, that in the (unintentional) event of default by the client, that the Islamic bank may have the power to maintain full ownership of the property as a collateral or risk management purposes. This may present an example as to why certain clients may prefer a *mushāraka mutanāqisa* as an Islamic financing tool.

To conclude this section, an enquiry was made to obtain an example of why a *mushāraka mutanāqisa* practice by the same Islamic bank would be altered from having a chain of three contracts to two contracts (or vice versa) from a Shari'a perspective. The interviewee explained, for example, that if a client seeks a finance for investment purposes (and therefore leases the financed property to a third party as an income generating activity), the Shari'a Supervisory Board viewed that leasing the share of Islamic bank A to the client would then be considered as 'a lease upon a lease'. Thus, solely selling the shares of Islamic retail bank A (through a gradual process) may therefore be more suitable in this regard.

4.1.2. Secondary Data for Islamic Retail Bank A: Annual Financial Statements

A review of the statement of financial position for the year ended 31 December 2018 of Islamic retail bank A indicates that Islamic retail bank A engages in *mushāraka mutanāqisa* transactions as a segment of its financing portfolio. This seems to be evident as the statement of financial position of Islamic retail bank A (for 2018) shows an entry on the assets side entitled 'financing assets'. The notes relating to financing assets indicates that the financing assets mainly consist of a *murābaha* and *mushāraka* (as opposed to *ijāra muntahia bil tamlik* that has a separate entry

within the assets category of the statement of financial position). The notes reveal that the 'mushāraka in real estates' amounts to around BHD 100 million and BHD 107 million for the years for 2018 and 2017, respectively. In line with the primary data, this therefore suggests that Islamic retail bank A engages in *mushāraka mutanāqisa* transactions by jointly partnering with clients to purchase real estates.

It may be noteworthy to mention two points in this regard. First, there seems to have been a decrease in amounts of *mushāraka* in real estates in 2018 relative to 2017. This may indicate that Islamic retail bank A may not have been active in executing *mushāraka mutanāqisa* transactions, because by doing so the entry amount may have increased rather than decreased. Thus, a decrease may suggest that the share of Islamic bank A may have been diminishing through the *mushāraka mutanāqisa*, without necessarily having a significant number of new transactions.

Second, the statement of financial position for 2018 reveals that total amount for *murābaha* transactions as a financing asset totaled around BHD 508 million for 2018, while *ijāra muntahia bil tamlīk* totaled around BHD 166 million. This may thus clearly indicate that the asset size of *mushāraka mutanāqisa* may be noticeably lower relative to other Islamic financial products. This may also suggest the notion that although *mushāraka mutanāqisa* is being practiced by Islamic retail bank A, it nevertheless seems to engage in this type of transaction on a noticeably smaller scale relative to other Islamic financial products.

4.2. Islamic Retail Bank B

4.2.1. Primary Data for Islamic Retail Bank B: Interviews

The primary data collection process for Islamic retail bank B revealed that the practices of *mushāraka mutanāqisa* by Islamic retail bank B was contrary to that of Islamic retail bank A, since it suggested that Islamic retail bank B does not engage in *mushāraka mutanāqisa* transactions. As a result, an enquiry was made regarding why *mushāraka mutanāqisa* was not being utilized as an Islamic financing product.

The primary data collection process revealed that generally, investors might not opt for this financing product due to possible various risks associated with a *mushāraka mutanāqisa*. For example, the results revealed that numerous methods might be used while implementing *mushāraka mutanāqisa* as a financing tool. One of them includes selling the shares of the Islamic bank to the client (through a gradual sale) at the market price during the execution of each sale (for example: contrary to a *murābaha* where the selling price is clearly stipulated at the start of the contract). Thus, interviewee responses suggested that not only was this considered risky from the perspective of investors (e.g. Islamic bank), but rather also from the viewpoint of consumers. The interviewee responses further suggested that many uncertainties seem to have been viewed by Islamic financiers (and perhaps consumers) as being associated with the *mushāraka mutanāqisa* product. To elaborate, both parties may tend to avoid engaging in *mushāraka mutanāqisa* due to the risks in market prices and/or uncertainties that may be associated with *mushāraka mutanāqisa*. Additionally, there seems to be other Islamic financial products that may be considered as more suitable than a *mushāraka mutanāqisa* (for example: *murābaha* or *ijāra muntahia bil tamlīk*). Thus, this product was not utilized by Islamic retail bank B.

There seems to be a distinction between the practices of Islamic retail bank A and B pertaining to *mushāraka mutanāqisa*. This may indicate that utilizing *mushāraka mutanāqisa* may not be necessarily considered as a main Islamic financial product utilized by the Islamic banking industry (for example: as opposed to a *murābaha*, which seems to be utilized by a majority of Islamic banks; according to financial statements), but rather an acceptable option that may be utilized if an Islamic bank chooses to do so. Offering such a product may be dependent on the preferences/opinions of an Islamic bank.

4.2.2. Secondary Data for Islamic Retail Bank B: Annual Financial Statements

The statement of financial position for the year ended 31 December 2018 of Islamic retail bank B may have indicated several factors that may be noteworthy.

First, an entry on the assets side included ‘financing assets’. The notes relating to the ‘financed assets’ evidences that financed assets consist of *murābaha*, *mushāraka*, and *ijāra muntahia bil tamlik*. Therefore, although there may be no indication of utilizing *mushāraka mutanāqisa* as an Islamic financing product, it nevertheless evidences the use of a normal *mushāraka*. This may be evidenced as *mushāraka* transactions totaled around BHD 130 thousand. Second, we compared the asset size of the normal *mushāraka* (and not *mushāraka mutanāqisa*) relative to other Islamic financing products for informative purposes. It was revealed that the financing assets for *murābaha* and *ijāra muntahia bil tamlik* (for the year ended 31 December 2018) amounted to around BHD 206 million and BHD 284 million, respectively. Thus, although Islamic retail bank B does not engage in *mushāraka mutanāqisa* transactions, we nevertheless highlight on the secondary data evidence that even the normal *mushāraka* transactions executed by Islamic retail bank B seems to be noticeably lower relative to other financing assets. As this is similar to the case of Islamic retail bank A, it may be suggested that the general practice of the Islamic banking industry relating to *mushāraka* transactions may be noticeably lower relative to other Islamic financial transactions (such as *murābaha* or *ijāra muntahia bil tamlik*). Third, to reiterate the abovementioned point, not only did the normal *mushāraka* (and not *mushāraka mutanāqisa*) be noticeably lower relative to other Islamic financing assets, rather the *mushāraka* entry for the year ending 2018 seemed to have decreased as well relative to the *mushāraka* entry for the preceding year in 2017. This may be apparent as the statement of financial position *mushāraka* for the year ending 2018 amounted to around BHD 130 thousand (as mentioned earlier), while it amounted to around BHD 291 thousand for the year ending in 2017.

4.3. Islamic Wholesale Bank C

4.3.1. Primary Data for Islamic Wholesale Bank C: Interviews

Similar to Islamic retail bank B, the primary data results suggested that Islamic wholesale bank C does not engage in *mushāraka mutanāqisa* transactions. The respective interviewee explained that as an Islamic wholesale bank, the bank has mainly two lines of businesses, one for private equity transactions and the other for yielding projects. According to interview responses, both lines of businesses did not require the engagement of *mushāraka mutanāqisa* transactions. Due to this finding, an enquiry was made in relation to the types of Islamic banking products Islamic wholesale bank C use for its transactions. Interviewee C mentioned that there were a number of products, including various forms of *ijāra*, *mudhāra*, and *wakala bil istithmār*. Interviewee C further added that one of the most used products was that of a commodity *murābaha*. This was because commodity *murābahas* are heavily used for treasury transactions, either to finance or borrow liquidity. As such, it seems that due to the availability of other Islamic financial products, Islamic wholesale bank C may have not been in need to utilize a *mushāraka mutanāqisa* product. This may further suggest the notion that the utilization of a *mushāraka mutanāqisa* as an Islamic banking product seems to be noticeably less utilized relative to other Islamic banking products. However, it may be difficult to generalize from a single case study that *mushāraka mutanāqisa* is relatively less used in the Islamic banking industry; rather, the empirical results seem to suggest that this may be the case.

4.3.2. Secondary Data for Islamic Wholesale Bank C: Annual Financial Statements

A review of the annual financial statements of Islamic wholesale bank C indicates that the responses obtained through the primary data collection process is similar to that of the secondary data collection process. This is because there seems to be no evidence in the financial reports to suggest that Islamic wholesale bank C had executed *mushāraka mutanāqisa* transactions. This may thus simply add validity to the primary data information.

4.4. Islamic Wholesale Bank D

4.4.1. Primary Data for Islamic Wholesale Bank D: Interviews

Similar to the cases of Islamic retail bank B and Islamic wholesale bank C, the primary data collection process revealed that Islamic wholesale bank D also does not engage in *mushāraka mutanāqisa* transactions. This thus supported the suggestion made in the previous sections that the utilization of *mushāraka mutanāqisa* might be considered as somewhat less adopted relative to other Islamic financing products.

4.4.2. Secondary Data for Islamic Wholesale Bank D: Annual Financial Statements

Similar to the case of Islamic wholesale bank C, a review of the statement of financial position for the year ended 2018 of Islamic wholesale bank D does not seem to suggest that the bank had executed *mushāraka mutanāqisa* transactions. This simply may have added validity to the primary data and supported the indications that *mushāraka mutanāqisa* may not be a widely used Islamic banking product in the Islamic banking industry.

4.5. Empirical Results Summary

The empirical data and analysis consisted of two for each Islamic retail and wholesale banks. The empirical results indicated that out of these four Islamic banks, solely one Islamic bank engages in *mushāraka mutanāqisa* transactions (Islamic retail bank A). This generally suggested the notion that *mushāraka mutanāqisa* as an Islamic banking product may be less utilized in the Islamic banking industry relative to other Islamic financial products.

There seems to be various reasons for the lack of utilizing *mushāraka mutanāqisa*, such as to avoid possible risks that may be associated with *mushāraka mutanāqisa*, or the existence of other Islamic banking products that may be viewed as more suitable alternatives. Evidence also tended to suggest that even for the case of Islamic retail bank A (which was the only bank that seems to engage in *mushāraka mutanāqisa* transactions), the statement of financial position for the year ended 2018 revealed that the asset size of *mushāraka mutanāqisa* may have been considerably smaller relative to other Islamic financing assets (for example: such as a *murābaha* or *ijāra muntahia bil tamlik*). This supported the notion that *mushāraka mutanāqisa* may be less utilized in the Islamic banking industry.

Figure 3 below illustratively displays the main empirical results pertaining to *mushāraka mutanāqisa* practices by the four Islamic banks used in this research as units of analysis:

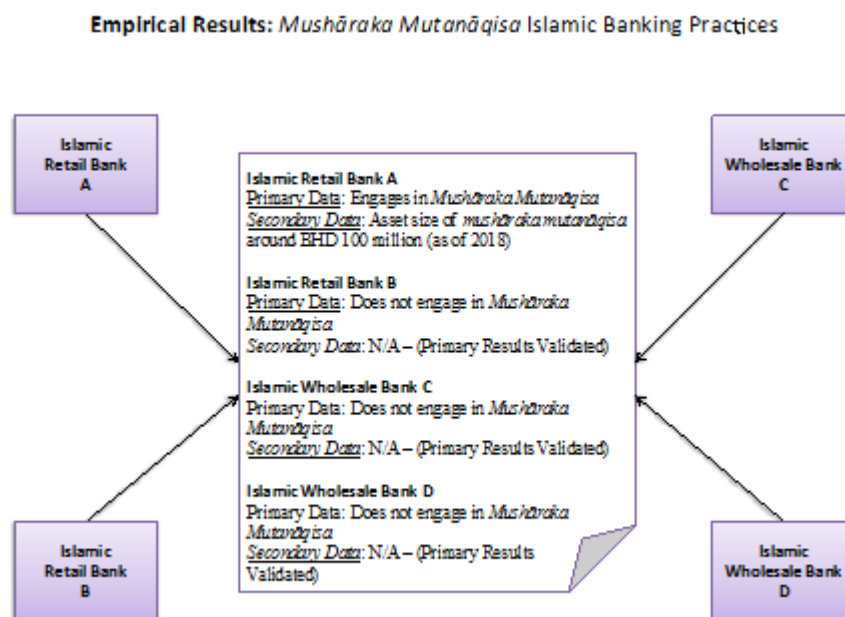


Figure-3. Empirical results summary.

There does not seem to be any indications that the practice of *mushāraka mutanāqisa* may increase in volume in the Islamic banking industry. It seems that the increase/decrease in the practices pertaining to *mushāraka mutanāqisa* may be dependent on certain stakeholders, such as the Shari'a Supervisory Board and management/consumers. These decisions seem to be dependent on the type of stakeholder. For example, the Shari'a Supervisory Board may opine on which Islamic financial instrument may be more suitable in specific cases from a Shari'a perspective, while both managements/consumers may do so from a risk management perspective.

It may be useful to suggest the notion here that when more than one Islamic financing tool exists for a single financing, such as a *mushāraka mutanāqisa* and *ijāra muntahia bil tamlik* (assuming the benefits/risks were equivalent in a certain case), it may be useful to set out a categorical strategy to choose the product that somehow benefits the economy and/or serves *maqāsid al-shari'a* (objectives of Islamic law) in a manner that may be considered as more beneficial. This may lead to a more efficient strategy when utilizing certain Islamic financing tools rather than others. However, the concluding empirical results do suggest that *mushāraka mutanāqisa* may be less utilized due to various risks perceived by certain stakeholders to be involved with *mushāraka mutanāqisa*.

5. CONCLUSION

Islamic finance uses several modes of financings, including sale, lease, and partnership. One of the forms of partnership (*mushāraka*) is known as *mushāraka mutanāqisa* (diminishing partnership). In a *mushāraka mutanāqisa*, an Islamic bank would jointly purchase an asset/property with a client as a partner, and thereafter sell its shares (e.g. on a gradual basis) to the client at a mark up price. This ultimately leads to the client attaining full legal ownership of the underlying property, while the Islamic bank would have retrieved its financing amount in addition to a permissible profit margin.

Evidence tends to suggest that there may not be much of a difference of opinions pertaining to the Shari'a permissibility of *mushāraka mutanāqisa*, as a sizeable majority of contemporary Shari'a jurists seem to view this product as permissible according to Shari'a. However, the empirical results suggested that this product might considerably be less utilized by the Islamic banking industry in the Kingdom of Bahrain.

To clarify, out of four Islamic banks used in this research as units of analysis (consisting of two for each Islamic retail and Islamic wholesale banks), solely one Islamic bank (Islamic retail bank A) engages in *mushāraka mutanāqisa* transactions. Evidence tends to suggest that the other three Islamic banks do not engage in *mushāraka mutanāqisa* transactions. Even for the case of Islamic retail bank A, the asset size of *mushāraka mutanāqisa* seemed to be noticeably lower relative to other Islamic financial products such as *murābaha* or *ijāra muntahia bil tamlik*.

Evidence suggests that although *mushāraka mutanāqisa* may be less utilized in the Islamic banking industry due to various reasons such as the preference of avoiding possible risks associated with this product, evidence nevertheless tends to suggest that there might be some positive attributes to a *mushāraka mutanāqisa*. This includes enabling a client to partially own an underlying property that may protect the client in the case of a (unintentional) default, whereby an Islamic bank may not be able to withhold full ownership of the underlying property to manage the risk of default.

There were a number of noteworthy limitations on this research. First, the practice of *mushāraka mutanāqisa* seemed to be somewhat less utilized in the Islamic banking industry. Thus, an in-depth explanation relating to the implementation of *mushāraka mutanāqisa* may have been limited. Second, as this research used multiple units of analysis, we recommend conducting a similar research on *mushāraka mutanāqisa* by selecting an Islamic bank that engages in *mushāraka mutanāqisa* using a 'single/holistic' case study design. By focusing on one unit of analysis for the empirical enquiry, this may reveal more information in relation to the practice and underlying philosophy of *mushāraka mutanāqisa*. We also recommend conducting similar researches using different jurisdictions for informative or comparative purposes.

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