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/ The entrepreneurial role of profit-and-loss sharing modes of finance: theory and practice

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The entrepreneurial role of profit-and-loss sharing modes of finance: theory and practice

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Abstract

Purpose

The purpose of this paper is to find out whether profit-and-loss-sharing (PLS) modes of finance have become viable financial alternatives for entrepreneurship and enterprise development or whether they are still merely an academic endeavour.

Design/methodology/approach

The method employed in this study is a combination of extensive examination of existing literature and critical analysis of the outcomes of several relevant studies in order to establish the convergent/divergent relationship between theory and practice in Islamic finance.

Findings

Based on available bank level and country level data, the paper presents evidence that the divergence between the theoretical perspective and the practical implementation of PLS modes of finance is widening to an alarming level. The paper argues that this divergence by no means can be attributed to the construct and the disposition of the PLS instruments; it is rather the product of the negative attitude and the lack of proper infrastructure of the majority of Islamic financial institutions (IFIs) – and their (reluctance) to accommodate entrepreneurship through the genuine implementation of PLS instruments.

Practical implications

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direction and the resilience of future research undertakings

should be focused on bridging the increasing gap between the prescribed role of PLS instruments and the actual performance of IFIs in promoting socio-economic development through the creation of a vibrant entrepreneurship sector.

Originality/value

The paper points out that while PLS models dominate the theoretical literature on Islamic finance, and whereas the majority of mainstream Muslim scholars and financial authorities overwhelmingly judge PLS models as being compelling financial options and practical developmental tools, the reality of Islamic finance paints a different picture. The paper emphasizes the need for IFIs to conform to their own charters and assume a leading developmental role in order to realize al-Shariah objectives (maqasid al Shariah). The paper identifies key research areas that warrant the attention of keen researchers with interest in the field of Islamic finance and entrepreneurship development.

Keywords

Profit-and-loss sharing (PLS) Mudharabah Musharakah
Entrepreneurship Small to medium-sized enterprises (SMEs)
Human capital Entrepreneurialism Finance Islam

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