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**How Islamic Banking System Work and Operate  
In  
Malaysia**

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**By**

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## Abstract

Malaysia has done very well in implementing Islamic Banking System in the country. There are mainly two types of problems involved in practising Islamic Banking System. The first one is theoretical problems and the second is implementation problems. The theoretical problems are very complex and varied, such as what an Islamic Banking System should be, how to define those Islamic financing terms, what's difference between "Interest" and "Riba", "Dividend" and "Interest", "Usury, Interest and Riba", "Backdoor Riba" and "Profit Margin". The implementation problems are "agency problems" in Al-Mudarabah, how to calculate profit margin in Al-Bai Bithman Ajil, Al-Murabah and Al-Ijarah financing without incurring "Backdoor Riba". Why practitioners prefer "Al-Bai Bithman Ajil" instead of "Al-Mudarabah" which is the core concept of Islamic Financing.

The study is aimed to understand how Islamic Banking System works and operates in Malaysia, what problems and challenges, Islamic Banking System is facing, and to examine whether Malaysian Islamic Banking System operating experience can be shared by other Muslim societies.

The study found that, the Islamic Banking System in Malaysia over its 10 year-evaluation period (1986-1996) performed very well and healthily, even though there were still some problems on modes of financing, too much debt financing instead of equity financing, agency problems in Al-Mudarabah, and not well enough the system operated Islamically. Unfortunately, the study also found that Malaysian experience in Islamic Banking System could not be shared by the Chinese Muslims in China.

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