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Individual Forex Trading Online: Shariah Issues

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Abstract

Forex trading, or also known as online individual currency trading, is one of the hot issues involving public awareness of the Islamic financial and economic system, and whether its implementation is Shariah-compliant or otherwise. Thus, this study aims to highlight Shariah issues related to individual Forex trading so that the public is not easily deceived by the luxurious offers that are often advertised by certain platforms or brokers. This qualitative research used the document analysis method involving journal articles, theses, magazines, newspapers, videos and slides to collect data, which were then analysed using the descriptive method. Findings show that there are several significant Shariah issues related to Forex trading, such as the absence of *qabd*, the existence of usury, gambling and *qard*. Findings also show that these issues could outrightly prohibit individual Forex trading despite there being tirades and guidelines adduced by various parties, such as academicians, traders or brokers, to legalize it. One implication of this study is that it is able to provide an understanding to the Muslim community so that they are not easily influenced by individual Forex trading in the name of profit. This study can augment the existing corpus of literature on the topic of foreign exchange.

Keywords: Individual *Forex*, Shariah Issues, Finance, Online

Introduction

Background of the Study

Foreign Exchange (Forex) in Arabic is called *al-sarf*, which refers to currency exchange, either an exchange involving the same currency or other currencies (Abdul Wahab, 2016). Forex Trading is a type of trade or transaction that trades the currency of one country against the currency of another country (currency pair) involving the main money markets in the world on a 24-hour basis (Ulil Amri, 2021).

The Forex market started in the 1970s when the first currency exchange took place (Zaki, 2012). At the time, an American citizen was allowed to travel to Europe and exchange USD for British pounds and vice versa. Currency exchange is a very simple process as it is only carried out by major banks and financial institutions. The first currency exchange took place in 1971 involving the US dollar and the Swiss Franc.

In this global era, the Forex industry is dominated by large institutions such as investment companies, banks or individual corporations. The Forex market is a vigorously expanding international market and can influence the global economy. Based on most of these trading platform websites, Forex trading is said to be a good source of income for individual investors and large companies. The Forex market is also open 24 hours a day, 5 days a week, and currencies are traded in pairs. It is one of the riskiest markets in the world because small changes in rates can cause significant losses for traders.

Among the currency trading that is still vibrant and attracting the attention of the community until today is online individual forex trading, as it promises to provide multiplied profits and luxuries. However, the majority of Islamic jurists and scholars have issued various fatwa stating that this trade is prohibited. Therefore, in order to understand the elements that have led to the prohibition of this trade, this study aims to determine the Shariah issues that have led to the prohibition of Forex trading and claim it to be illegal (*haram*).

Problem Statement

The economic downturn has forced certain sections of the community to desperately seek multiple sources of income. Furthermore, the Covid-19 pandemic has caused some sections of the community to lose their jobs, which in turn means losing their monthly income too (Farhan et al., 2021). This situation provides an opportunity for brokers/platforms to post advertisements on Facebook or YouTube that depict how easy it is for people to earn money through online individual Forex trading. Similarly, Forex investment schemes, like GCG Asia Forex Investment, informs their investors that their money will be invested by GCG Asia companies in various mediums to generate huge profits. Investors will be given an investment website link along with a password and they will be able to monitor the amount of profit they receive. However, these benefits cannot be transferred or redeemed.

This individual Forex trading scheme has been vigorously advertised lately and it seems to be sprouting like mushrooms as celebrities and influencers have already started promoting this trade. This is because their luxurious lifestyles are paid for by the money obtained from Forex instruments and they had uploaded photos and videos of their lifestyles, such as income in USD, luxury homes and luxury cars, in their social media. Hence, it is certain that many of their followers on social media who have no knowledge of this trade will be fascinated and flock to participate in this trade.

In addition, there are also communication media such as Telegram, namely the No.1 Forex Telegram in Malaysia, that often attracts people to join this group. This is also the reason why the community is increasingly interested in trading using this platform, especially students. According to Fazli (2020), students in Higher Institutions of Education (IPTs) have been attracted to Forex investments and have become quite apt in it. This is because the transaction is easy to complete anywhere, either at home or in an internet cafe. The application only requires the use of a computer or smartphone with internet access to carry out transactions. This 24-hour open market provides convenience to Forex traders, namely students or those who do it part-time after their working hours. Some have even quit their jobs due to the double profits from this trade.

Although majority of the views state that Forex trading is prohibited (*haram*) due to elements of cheating and other deceptions, however, many are still interested in joining it. One view from an expert in Islamic finances, Aznan Hasan, was that, "Most online brokers are dishonest, only 10% are genuine, 90% are mere speculation and the currency/gold does not exist for a particular transaction" (*Aznan,* 2015).

According to Eza (2020), those who participate in individual Forex trading are actually, on average, aware of the prohibition of such transactions. However, as a result of being overly influenced and duped by brokers and traders in this field, they are willing to ignore and disparage the fatwa issued by muftis and Islamic authoritative experts around the world.

There are also various websites created by brokers and traders to present their personal views on the arguments and fatwa related to the prohibition of Forex trading (Ridzcode, 2021).

Therefore, this study aimed to examine Shariah issues related to online individual Forex trading and keep the public informed so that they are not easily deceived by the profits promised by brokers, traders and trading platforms.

Literature Review

Currency Trading *(Al-Sarf)*

Based on previous studies, *bay 'al-sarf* is a contract of exchange involving money for money. Since these contracts can be easily manipulated for the purpose of generating loans with interest, which is prohibited in Islam, hence, these contracts need to be closely monitored. These contracts are a mechanism in foreign exchange involving the conversion of one currency unit into another currency unit. As a sale and purchase contract, the general conditions of sale and purchase also apply to the *bay 'al-sarf* contract. The terms of sale and purchase include (Norhaniza, 2018)

(a) Condition for forming a contract *(in'iqad)*
- Conditions for the contracting parties – sane and mature, and involves two parties
- Conditions of the contract – acceptance must be equal to the offer
- Condition for the place of the agreement (akad) – the ijab and qabul ceremony
- Conditions for the goods in the contract – present/exist, of value, under the control of the owner (seller) and can be surrendered during the contract.

(b) Condition for the implementation *(nafaz)*
- Own or have the power to administer – ability to sell without any hindrances

(c) Valid condition – free from defects
- Due to ignorance, coercion, deferment, *gharar*, danger and defect in the conditions – only one party obtains the benefits.

According to the National Fatwa Council under the Islamic Religious Affairs of Malaysia, the specific conditions for *bay' al-sarf* are as follows:

1. *Taqabbudh* (surrender) of both goods/items involved in the forex platform before both parties to the transaction exit the *aqad* ceremony;
2. Currency trading must be carried out in a *lani* manner and there cannot be any deferment; and
3. The *al-sarf* (sales and purchase ceremony) must be free from *khiyar al-Syart*.

Shariah Law (Hukum) Related to Online *Forex* Trading

Previous studies have stated that Forex Trading is one form of trading that exist today whereby it is no longer carried out by certain groups but by individuals. They carry out Forex trading only to make a profit by buying a foreign currency then keeping it, and selling it when the value of the currency goes up. Therefore, legal provisions obtained through the method and study of *fiqh* are as follows (Khosiah, 2020)

a) First: *Forex* is permitted due to the need to buy and sell currency in order to make export-import trade payments by one country to another based on existing conditions.
b) Second: Forex is prohibited if it is carried out solely to gain profit without trading goods or commodities.

Based on previous studies and discussions, it can be concluded that although the majority of ulama permit online Forex trading, it must be carried out according to strict criteria and conditions. Among the conditions are that there is no speculation, no rollover interest, no broker fees for opening positions that exceed yesterdays, and no higher spread rate chargers to substitute the rollover interest. Hence, if these terms and conditions are not met then online individual Forex trading becomes illegal and this is supported by a fatwa issued by the Indonesian Ulama Council (MUI) (Rafiqah, 2020).

Methodology

Study Design

This study adopted the qualitative study design, which is the most important element in a study.

Data Collection Method

This study used the document analysis method for data collection purposes because document or content analysis can provide an objective and systematic explanation of information that exists in literature, such as in journals, theses and previous studies. In addition, the study also referred to official websites such as the website of the Mufti's Department to examine laws related to the research topic as well as the website of the Forex platform to explore trading operations. This study also analysed the websites of brokers and traders to examine their arguments against the prohibition of Forex trading. In addition, YouTube video clips presented by Islamic finance experts such as Hasan and Rahman (2021), were also examined to increase an understanding of the topic in study. Newspapers and magazines were also examined to learn about the latest issues related to Forex trading to further strengthen this study.

Data Analysis Method

This study used a descriptive method for data analysis because the main focus of a descriptive research is to answer the 'what' question in the course of the study. Therefore, this study tried to answer the question, "what are the Shariah issues related to online individual Forex trading online" by discussing in detail the implementation of Forex instruments that resulted in their prohibition.

Findings and Discussions

Shariah Issues in Individual *Forex* Trading

From an Islamic perspective, this study found that there were several Shariah issues that led to online individual Forex transactions becoming invalid and void based on the following elements:

1. Absence of *Qabd* in Currency Trading

Online individual Forex trading is carried out by opening a position (open position) against the selected instrument. This operation ends by closing the position (close position) against the instrument (Zaki, 2012). For example, a trader wants to open a long position against the EUR/USD instrument where the trader will buy Euro currency by paying USD dollar currency. The *qabd* demanded from this transaction from a Shariah perspective is

1) The trader must surrender the USD to the broker: and
2) The broker must surrender the EUR currency to the trader

However, online individual Forex trading is the opposite and contrary to the demands of *qabd* mentioned in the Shariah. This issue is evident when a trader buys a long position against the EUR/USD at a price of 1.4500 for 10,000 units and then the trader closes the position at a price of 1.4550 and the trader makes a profit of 50 pips. In this transaction, when the trader opens a long position, the trader is considered to have bought EUR10,000 by making a payment of USD14,500 (Marjan et.al., 2011). Then, the trader resells the 10,000 EUR with a profit of USD14,550. Hence, the trader earns a profit of USD50.

The above individual Forex trading transactions indicate an absence of *qabd* because the currency purchased by the trader cannot be credited immediately by the broker into the trader's account. Therefore, traders who open purchasing positions on EUR/USD instruments will not be able to make *qabd* on the purchased EUR currency indefinitely. In this case, the trader will not be able to enjoy all the benefits from the increase in the currency's price and the trader cannot make withdrawals (money) as long as the position opened by the trader is still left with an OPEN status. This continues and the price or value remains floating until the trader CLOSES the position or in other words, the trader resells the currency purchased earlier.

It is obvious that the absence of *qabd* in online individual Forex trading transactions appear in four situations, i.e.

1) A currency that is purchased when a trader opens a position will not be credited into the trader's account until the said currency has been re-sold to a broker when the position closes.
2) The profit that is obtained from the increase in the price of the currency bought earlier can only be paid in USD.
3) When a trader closes a position, he will resell the currency he bought from the broker, although he is yet to commit *qabd* against the currency he bought. This means that the trader is in fact selling Euros that he does not own and not in his possession when he takes a position to sell the EUR/USD because what he has in the account is only the USD.
4) Trading that uses cross currency pairs involves two *sarf* contracts simultaneously. For example, the GBP/JPY currency refers to buying the pound currency by paying in yen currency in addition to having USD deposit money in the platform. According to tradition, the transaction has to involve two different *sarf* contracts. However, in this Forex platform, the trader will press only one button (long), and the USD will be exchanged for yen and the yen will be exchanged for pounds. When the position is closed, the pound is converted to yen and the yen is converted to USD at the same time and this involves two more contracts that occur simultaneously. Therefore, there is no *taqabud* during the first and second transactions, which means each involve two simultaneous *sarf* contracts and make it look like there are four simultaneous *sarf* contracts. Selling currency is illegal because no *qabd* takes place, either physically or legally.

The Existence of Speculation and Gambling

Acknowledgment by most platforms/brokers that offer online Forex trading will be made through "Risk disclosure/risk warning", which indicates that Forex trading involves a high degree of risk (Rahim & Nurliyana, 2021). The risk exposures that are commonly displayed on the websites are as follows:

- *"Trading foreign exchange on margin carries a high level of risk and may not be suitable for all investors. The high degree of leverage can work against you or for you"* (Daily FX, t.th).
- *"Forex trading involves substantial risk of loss and is not suitable for all investors".*

The above statement clearly shows that individual Forex trading is a trading transaction that has no guarantee of either profit or loss. Thus, this type of trading is based on speculation and there is a high risk of losses incurring, which is prohibited by Shariah. Currency trading, in which the currency is yet to be legally owned is presumed to be a speculative element (Rahmat et. al., 2021). The Prophet SAW exhorted:

"O people who believe! Verily liquor, gambling, idol worshiping, and gambling with arrows are heinous deeds and the work of the devil, so stay away from those (deeds) so that you will reap the benefits"

(Riwayat Abu Daud)

Speculation is often associated with short-term investments and attempts to bet on a rise in the prices of stocks or assets can lead to extreme risk or gambling (Kunhibava, 2014). Although according to Islamic law the existence of speculation does not prohibit a transaction, it can be prohibited if it involves excessive uncertainty and risk, in addition to any element of gambling. Therefore, gambling and speculation are among the elements found in individual Forex trading because this trading results in only one party making a profit while the other incurs a loss. Individual Forex operations depend on currency market price fluctuations and the parties involved will speculate on prices to make a profit, to the detriment of the other party.

Existence of *Qard* in *Leverage*

Leverage involves borrowing an amount of money needed for investment purposes. In the case of Forex transactions, the money is usually loaned by a platform. This leverage facility aims to provide opportunities for forex traders in order to obtain greater profits. The leverage ratio is usually 50:1, 100:1, 200:1 and so on. This depends on the platform's capability and the amount of capital (investment) adduced by the trader. For example, 100,000-units of a currency is the amount to be traded and the leverage provided to traders would be 100:1. This means the trader only needs to provide 1,000 units of currency with a 100:1 leverage facility (Zamerey, 2009).

In individual forex trading, the broker loans to the trader and the loan provides benefits to the broker. Hence, traders who obtain a loan will definitely open a forex position through the broker. In forex transactions between traders and brokers, the broker will make a profit through the spread, which is the difference between the bid price and the asking price (FBS Online Forex Broker, 2021). This means that brokers sell currencies to traders at high prices, and buy them at low prices.

Therefore, this leverage is included in the loan (*qard*), which benefits the lender and this element is prohibited in Shariah because every loan that provides benefits to the lender is considered a form of usury (*riba*). This section of jurisprudence is famously used in the discussion of *riba*, whereby: "*Every loan that benefits (the lender), is riba*". Nevertheless, although according to the science of hadith, it is a hadith that is not confirmed as an authentic *sanad*, however, it has become a method agreed upon by all Muslims."

Existence of *Al-Nasiah* Usury in *Rollover Interest*

The rollover interest issue is the most significant Shariah issue in Forex trading. This occurs when an individual opens a position that is greater than the overnight one. This will expose him to accept or give *riba al-nasi'ah*, which is forbidden by Shariah. This is according to the exhortations of Allah SWT in Surah al-Baqarah: 278-279, which means, "*O ye who believe! Observe your duty to Allah, and give up what remaineth (due to you) from usury, if ye are (in truth) believers. And if you do not, then be informed of a war [against you] from Allāh and His Messenger. But if you repent, you may have your principles - [thus] you do no wrong, nor are you wronged".*

Discussion of The Findings

Based on all the issues that have been discussed in this study, it is clear that Forex trading is against Islamic Shari'ah. This is supported by the 98th Muzakarah Fatwa Committee of the National Council for Islamic Religious Affairs of Malaysia (MKI Muzakarah Committee), which stated that online individual Forex trading is illegal (*haram*). The committee also emphasized that this fatwa does not apply to foreign currency exchange transactions over the counter at licensed money changers or similar transactions conducted by financial institutions licensed under Malaysian law (Jakim, 2012).

However, there have also been various Shariah-compliant Forex schemes (Islamic Forex) of late that offer Forex trading without leverage as they claim to apply the *qard hasan* concept. It is said that implementation of these schemes does not obtain any benefit from the leverage lent to traders. However, even if it is true that the loan transactions do not offer benefits and there is no element of usury (*riba*), but the existence of other Shariah issues still remain in the transactions. Shariah issues such as *qabd* and fixed gambling cannot be eliminated in these Shariah-compliant Forex transactions. Zero rollover interest is also offered by Forex schemes that claim their transactions are Shariah compliant (Alisa, 2014).

Thus, it can be concluded that any Forex transaction, even if it is claimed to be Shariah compliant, could not be completely Shariah compliant. Therefore, Shariah-compliant Forex transactions still do not exist until today even though they have incorporated the *qard hasan* and zero rollover interest concepts.

Conclusion

In general, currency trading is a trade that considers currency as a "commodity". This principle is likely to be in conflict with the Shariah principle, which does not attach value to currency other than as an intermediary for trade exchange. Online individual Forex trading indicates that there are various Shariah issues that arise resulting in this type of transactions becoming illegal, either carried out by traders or brokers. These Shariah issues include the absence of *qabd* in currency trading, existence of elements related to speculation and gambling as well as the existence of *qard* in leverage and *riba al-nasiah* in rollover interest.

Although there are still those who claim that the transactions they have carried out are Shariah-compliant Forex transactions due to the existence of *qard hasan* and the absence of rollover interest; however, it does not mean that these transactions are automatically Halal because there are still other elements of prohibition that all parties concerned need to observe. Therefore, the Muslim community must be careful in choosing a trading platform and must refer to knowledgeable individuals in Islamic finance if there is any doubt in the transactions carried out.

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