REFORMING MONEY AND BANKING

We often speak about the rapid rise of poverty in Pakistan and across the globe. Poverty is consistently rising at an alarming rate; despite this, limited attention is paid to its fundamental cause: unequal distribution of wealth and resources. Conventionally, poverty is linked with overpopulation, agricultural problems and poor governance; however, these explanations remain incomplete. As a society, we have often failed to recognize a root yet ignored factor, which is linked to how money is created, managed, distributed and controlled .This is the responsibility of a bank in almost every country; as a result, a strong banking structure plays an important role in overcoming these growing problems.

This essay argues how reforming our banking system into full-reserve and interest-free banks can help control inflation, poverty and other economic problems. To understand the importance of these reforms, it is necessary to first examine how money is created within *the* modern banking system. Modern banks make money primarily through lending. In other words, banks create money by issuing loans, which adds new digital money to the economy without transferring existing cash. When a person borrows a loan from a bank, the bank provides the loan in the form of digital money. Although this may sound unusual but it actually occurs. However, when someone wishes to withdraw the money from an ATM or any source the bank has physical reserves, which store some amount of money to meet normal daily withdrawals. Physical reserves are maintained by a bank, This provided information also answers another very common question which is "How banks run out of money?" This is because the physical reserves of the banks are limited. Since most transactions are now conducted digitally so this system is implemented even more effectively however, physical cash is still important. The amount of money a commercial bank can create is regulated by central banks, ensuring that excessive loans does not affect the economy.
Government also takes debts from the banks to improve infrastructure, pay salaries and to run the country and they have to pay back the debt along interest. Even if the government has the amount they borrowed, sometimes due to the large amount of interest it is unable to return repay it. As a result, the debt increases and eventually the interest burden also increases.***" Pakistan's 2025-26 budget allocates ~Rs 8.2 trillion for debt servicing which includes interest payments and principal repayment***"**.** To manage the debt and interest the Government have to pay it from taxes, fines and sometimes by borrowing more and this is where the debt cycle or cycle of borrowing starts. When the government continues to borrow excessively, the prices of goods and services may rise, causing inflation worsening the poverty. However, this is not the only reason for inflation. When Government continues to borrow as a result more money is created, while the quantity of goods remains same. More people chase the same goods so as a result the prices increases rapidly. This situation affects the poor people and again poverty gets worse. As most of the money is spent on interest payment, less money is left to be spent on education, infrastructure , health and transport. This excessive borrowing can make the imports even more expensive. Also customers deposited money is not the only way bank pays the loans; it also borrows from other banks. *As banks creates money through lending instead of using exiting deposits, these excessive lending and government borrowing can expand money supply too quickly.*

These discussed problems calls for an immediate reforms in Pakistan's banking sector. As the good health of our banking sector is very crucial for the economic growth for the development of Pakistan. A weak banking system can therefore, affect our economy, erode people's trust and increasing poverty hence, a strong banking system must be responsible and people-friendly.

One proposed reform is adoption of full-reserve system, In such system the banks keep 100% instead using them to make loans or investments, this system is very strong, secure, stable and people-friendly and have several benefits.

HERE ARE SOME OF THE ADVANTAGES OF FULL-RESERVE SYSTEM LISTED BELOW:

In a full-reserve system, the government can borrow responsibly because it could borrow from the existing money in the banks. No new money can be created because banks could not lend deposits*.* The bank must keep 100% of a depositor*'s funds as reserves instead of lending them.* As a result, all the money will be available at any time, preventing bank collapses and reducing the chances of bank runs. Because banks can always return deposited amounts , hence a safer environment will be developed between the bank and the depositors. People will trust the banks, seeing them as the only safe place for their money. Full-reserve system promotes financial stability. It also plays an important role in overcoming the problems such as poverty. It also controls inflation by preventing the banks from creating extra money. It also enhance confidence in depositors ensuring them there money is fully backed and available at any time.

Besides reforming our banking system into a full-reserve system, several other reforms can be adopted such as elimination of interests (riba) and transforming our banks into interest-free banks. Interest-free banks , also known as Islamic banks ,they are operated on the principal of profit-and-loss sharing. In such banks when money is deposited instead of lending it on interest the bank uses it to invest in business, trade or other projects. The profit and loss from the investments are shared between the depositor and the bank. If the business succeeded, the profits are shared; if the business fails the loss are shared. Now the question arises "Do they offer financing? Yes, of course they offer but it operates on the same profit-and-loss sharing principal now question comes how? For example, if we want to start a business and ask the bank for some loan they invest in the business under profit-and-loss sharing contract, so an investment contract is always signed.

SOME OF THE ADVANTAGES OF INTEREST-FREE BANKS ARE LISTED BELOW:

In comparison with an interest-based system, the interest-free banking system is more people-friendly and avoid charging interest(riba). In such system, the government debts does not increase rapidly due to interest costs. It provides opportunity for investment to everyone without burdening them with heavy interest payments and eventually reducing financial burden on borrowers. There is a stronger partnership between bank and depositors, and this system can lead to greater economic stability while protecting people from heavy interest-based debts. It is a risk-sharing investment rather than speculative a debt accumulation

Both of these systems can reduce government debt because they encourage the government to borrow responsibly system and only for essential purposes ,Currently Government are borrowing extensively from the IMF and commercial banks either for national development or to repay the debts. Interest-free banks can reduce the interest on the Government which is rising rapidly each year. In addition, adopting these reforms and switching to them directly is not very easy and will take considerable time. As many banks heavily rely on existing fractional-reserve and interest-based system as they are • generating substantial daily profits daily. Therefore, switching directly to these new systems directly can lead to financial unstability. Regulation of such system also may take a lot time , as many people are unaware of profit-and-loss sharing concept so giving them education about this system is a must thing and is very essential. This system will require qualified professionals as Islamic banking contracts are more complex and require expertise in both Islamic and modern banking

It is also important to discuss the common misconception which is that many individuals people halal transaction generate minimal profit and due to this belief they have polluted their lives by un-islamic sources of income. In my opinion that is not always true everything depends on proper planning and how well an investment is actually planned and structured. Profit-and-loss sharing depends on investments as discussed earlier. These type of system truly relies on investment-based contracts where not only profits are shared but also the loss are shared equally as well. Therefore it provides a good opportunity of investment for an individual who wish to invest instead of going for methods of earning that are un-islamic. For example, meezan bank is known to be largest Pakistan Islamic bank which has experienced a strong growth.

In conclusion, the current banking structure of Pakistan has played significant role in contributing to economic challenges, including rising poverty, inflation, and unsustainable government debt. Current banking system which relies heavily on fractional-reserve banking and interest-based lending that promotes unequal distribution of money. Transforming the banking system through full-reserve banking and interest-free (Islamic) finance offers a promising and sustainable path towards reducing poverty, controlling inflation, strengthening financial stability, and development of economy. fortunately these reforms are not only theoretically sound but are already being adopted practically and implemented. These reforms have a strong potential to build a more stable and socially responsible economic environment.