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Introduction: continuing the debate on Islamic finance

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With the second of a third-article series, the new issue of our *Review* continues the debate on Islamic banking that had started already in the old series of the journal.[1] As Askari, Krichene and Mirakhor (2014) highlight, the issue is of high topicality especially in Europe.

As is well known, the Old Continent has embarked in a medium-term economic policy based on three pillars: restrictive fiscal policy, expansionary monetary policy and "structural reforms". The last pillar translates into a number of counter-reforms mostly aimed at increasing net exports through lower wages (that should increase cost-competitiveness and, hopefully, price-competitiveness) and attracting foreign direct investments.

This is not the place to restate the obvious, i.e. the two mentioned objectives are very difficult to be reached simultaneously, as trivial balance-of-payments accountancy shows. Rather, in the conservative view the link between them is obvious: austerity measures aimed at containing domestic demand imply that if investments are to be implemented at all (and one would not see why should firms invest, in such a stagnating environment), they must be financed from abroad.

The Keynesian critique of such position is obvious: austerity is self-defeating and should be abandoned altogether. However, given the manifest political difficulty in reaching such much-needed objective, any source of demand must be welcomed, evidently including foreign direct investments.

There is thus 'bipartisan' agreement at least on this limited short-term objective. Hence, besides the fundamental ethical, religious and philosophical dimensions raised by Islamic finance – connected e.g. to what role should finance play in our societies – the immediate policy

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[1] The first article was published in the past issue: see Askari and Krichene (2014),

relevance of the debate around it rests in the on-going competition among developed countries to attract financial capital from abroad.

With this three-article strong contribution, the *Review* wishes to further the debate specifically on the economic feasibility of making the entire financial system Sharia-compliant. Indeed, while limited market niches may (and probably will) be further developed outside Muslim countries anyways, a more radical reform at the systemic level is advocated for by the authors of the series that will end in the forthcoming September issue. Evidently, this is not necessarily the position endorsed by the *Review*, but it seems one worth debating.

For example, – again, independently of any moral or religious consideration – an objection from a Keynesian standpoint, already raised in D'Ippoliti (2014), concerns 100% reserve banking. The topic is incidentally dealt with also in the last article of the current issue, dealing with some early writings by Minsky on macro-prudential regulation. As Kregel (2014) notes, citing Neil Wallace, such proposal "eliminates the banking system", in the sense that it rules out endogenous money supply in the retail banking sector. The point was already discussed by Askari and Krichene (2014), who on the contrary see the impossibility for banks to create purchasing power "out of think air" as one of the very advantages of an Islamic system, because it may reduce financial speculation and the disconnection of finance from the real economy.

Finally, the second article of the issue focuses again on the Eurozone crisis, a cause of concern for the whole global economy. In his contribution, Botta (2014) examines the options for industrial policy as a means to revive economic growth, arguing for a distinctly interventionist stance. To this end, a wide battery of industrial policy tools should be considered ranging from subsidies and fiscal incentives to innovative firms, public financing of research and development, sectoral policies, and public procurements for home-produced goods. We stress that future European Union (EU) industrial policy should be regionally focused and specifically target structural changes in the periphery as the main way to favor center–periphery convergence and avoid the reappearance of those external imbalances that many consider as a crucial cause of the current crisis.

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