



Using Forward Exchange Contracts as A Hedging Tool

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<QUESTION>

My company has massive purchases and billings in foreign currency. We use forward foreign exchange contracts as a hedging tool i.e. we agree on future exchange rates at specific dates with the bank whereby we have the obligation (not the option) to use the rate at the exercise date. This is to reduce our risk of loss on exchange for the company. Is doing these types of transactions in good faith for the benefit of the company considered halal?

<ANSWER>

In the name of Allah, Most Compassionate, Most Merciful,

As explained previously in a detailed answer titled "Foreign Exchange Trading" that Hedging and all 'futures' transactions are impermissible in Shari'ah, because they contravene one or more of the principles of a valid Islamic transaction.

To use forward foreign exchange contracts as a hedging tool is not permitted. According to Shari'ah, a sale must be instant and absolute, and can not be attributed to a future date. If a sale is attributed to a future date or is contingent on a future event, it will become void. Yes, one can promise to sell on a future date, but a new separate deal based on offer (ijab) and acceptance (qabul) will have to take place. All the jurists (fuqaha) are unanimous on this established principle of Shari'ah.

Another reason for the impermissibility of such transactions is that they fall in the category of exchanging a debt against a debt which is also prohibited in Shari'ah. In transactions attributed to forward dates, both the commodity and price are deferred making the transaction into one where a debt is exchanged against a debt.

Sayyiduna Abd Allah ibn Umar (may Allah be pleased with him) narrates that the Messenger of Allah (Allah bless him & give him peace) prohibited the selling of a debt in return for a debt (bay al-kali bi al-kali). (Sunan al-Bayhaqi 5/290, Sunan Daraqutni 3/71, and Mustadrak al-Hakim 2/57)

And Allah knows best

Muhammad ibn Adam

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