Salam - Forward Sale Contract

Overview

Salam is a forward sale contract permitted in Islamic finance where payment is made in advance for goods to be delivered in the future. The Prophet Muhammad (peace be upon him) specifically permitted it to serve the financing needs of farmers and manufacturers.

Definition

Salam is a sale contract where the buyer pays the full price in advance and the seller commits to deliver specified goods at a future date.

Shariah Requirements

Full Advance Payment - The entire purchase price must be paid at contract time in cash

Precise Specification - The commodity must be described with complete clarity (type, quality, quantity)

Commodity Available at Delivery - Must be generally available in the market at maturity

Specified Delivery Date - Clear delivery terms with specific date

Cannot Be Gold, Silver, or Currency - These require immediate exchange

Practical Applications

Agricultural Financing

Farmers need funds for seeds and equipment. Buyers pay upfront for post-harvest delivery.

Manufacturing Financing

Manufacturers receive advance payment to produce goods like textiles or furniture.

Working Capital

Islamic banks use parallel salam to provide financing to producers.

Advantages

For Sellers: Immediate working capital, production certainty, price security

For Buyers: Price security, supply assurance, potential profit

For Banks: Shariah-compliant financing tool, profit opportunity

Key Takeaways

- Salam is an Islamic forward sale with full advance payment
- Requires precise commodity specification and defined delivery
- Used for agricultural and manufacturing finance
- Parallel salam allows banks to profit while financing production
- Main risks are delivery failure and quality disputes