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THE IMPORTANCE OF IMPLEMENTATION OF ISLAMIC FINANCE PRODUCTS TO COMMERCIAL BANKS

Z.Shodmonov – MBA, Banking and Finance Academy of the Republic of Uzbekistan

Abstract

Many studies have been conducted on the scientific basis of Islamic finance, the role of this financial sector in the banking and financial system of the world countries, its development trend and future forecasting, and these works are being continued intensively. The research also explores issues such as strengthening the global share of the Islamic finance sector and leveraging its full potential and increasing its assets. In the development of Islamic finance in the world, it is necessary to conduct scientific research on the regulation and coordination of all issues related to this topic, as well as to study the level of influence of this system on the world economic development on a large scale.

The Islamic banking system was founded in the 1970s. In a short time, it has become an integrated mechanism that can fully compete with commercial banks. Unlike commercial banks, Islamic banks attract entrepreneurs and businessmen through a profit and loss sharing system (credit system). This system attracted not only Muslims but also representatives of other religions with its fairness and low level of financial crisis. In recent years, the total assets of Islamic financial institutions have grown by 15-20% per year and reached 2.5 trillion dollars. Therefore, it is important to attract funds from existing banks, investment funds and companies based on Islamic finance in developed countries in order to support the private sector and socio-economic development of Uzbekistan.

Keywords: commercial banking, Islamic banking system, traditional banking services, mudoraba, resource, partnership, diversification, Islamic principles.



Introduction. Uzbekistan is a developing country with the largest population in Central Asia. Many people understand that in our country, where more than 90 percent of the population is Muslim, there is an opportunity to introduce the Islamic financial system as an alternative to the traditional banking and financial system. Attention is being paid to investment attraction, introduction of alternative financing institutions and tools in Uzbekistan. The task of expanding the scope and improving the quality of banking services has been set in the republic at the expense of attracting advanced international experience and technologies. In order to fulfill this task, it is necessary to mobilize the funds of foreign investors and residents of the country that are not involved in financial relations into the economy through the establishment of alternative financial institutions, to base proposals and recommendations on the integration of Islamic financial institutions into the country's financial system, to implement financial transactions operating in accordance with Islamic principles, and in traditional banks. Organization of "Islamic products" is one of the most urgent issues. Introducing the Islamic finance sector as an alternative to the current banking and finance system in our country can be one of the main solutions to the existing problems and bring some positive results.

In contrast to commercial banks, Islamic banks were able to attract business representatives through the means of distributing profit and loss among participants based on the principles of fairness and humanity. This system has attracted not only Muslim developing countries but also governments of other developed countries due to its fairness, low level of risk and low level of financial crisis. The banking sector based on Islamic finance is rapidly developing and recognized in the world as an alternative system to the current banking sector and has become a complete financial system competing with traditional banks in about half a century.

Due to the significant increase in interest in Islamic finance products in Uzbekistan in recent years, the scope of conducting scientific research and practical work in this field, in particular, aimed at attracting a limited amount of murabahah and lease financing lines from the Islamic Development Bank and its group of organizations, has increased. However, the tools and products used

in the Islamic banking and financial system are few in our country because the basis of the regulatory and legal documents necessary for the implementation of Islamic banking and financial services and products by local financial institutions has not been developed. But such products are offered by a group of secretive market participants, in which contracts and products are sold that are intended only for the benefit of the commercial side. In addition, since the majority of the population believes in this, it is the reason for the consumers to get into a big loss. Therefore, we believe that the time has come to develop measures to establish an Islamic financial system in the country. In this regard, the President of the Republic of Uzbekistan in his address to the Oliy Majlis on December 29, 2020 stated that the time has come to create a legal framework for the introduction of Islamic financial services in Uzbekistan, and that expert from the Islamic Development Bank and other international financial organizations will be involved in this. Before integrating this system into the current banking and financial system in the country, a comprehensive assessment of its impact on the population's well-being and business development is required.

Islamic banking refers to a banking system that follows Islamic law in its core operations. It has similar objectives and operations to conventional banks. However, the guiding principles of Islamic banking are mutual risk and profit sharing between the parties, ensuring fairness and justice in any transaction and business transaction. Activities related to usury, gambling and speculative trading are prohibited by Islamic principles. The establishment of Islamic banking was mainly due to the demand of Muslims for interest-free financing products and services from financial institutions. Since its inception, due to its rapid growth, many conventional banks have launched their Islamic banking windows around the world. Over the past decades, Islamic banking has played an important role in the growth of the international financial system.

Literature review. In the field of world science, Islamic finance is a relatively new direction, but many studies have been done. Muhammad Umar Chapra (2009) was one of the first to focus on crisis tolerance, which is considered the most important aspect of Islamic finance, in his research. This article argues that insufficient market

discipline in the financial system, excessive lending, and high leverage eventually lead to a crisis. It was also noted that risk-sharing, first lending for the purchase of real goods and services, and limiting the sale of debt, followed by short-term trading, excessive uncertainty (gharar) and gambling (maysir) could help strengthen discipline. This can significantly reduce financial instability. All these are embodied in Islamic finance.

Jocelyn and Labidi (2021) noted that there is a growth in Islamic finance around the world. In the global financial and economic crisis, Islamic financial institutions have shown a significant degree of resilience compared to traditional financial institutions. The research examines the current state of risk management in Islamic banking, Islamic investment funds and Islamic finance. Special emphasis is placed on the annual growth of Islamic finance by 15-20 percent. Among the local scholars, Abrorov (2023) conducted many studies on Islamic finance, in which the general development trends of Islamic finance were analyzed in terms of periods, regions, countries and financial sectors. Scientific works are mainly devoted to the study of Islamic securities - sukuk.

Analysis. Various information and comments were used during the preparation of the article. This information is based on Islamic finance, financial trends, ethical finance, technological advances and other such areas. Based on the information obtained in the article, he extrapolates the development of Islamic finance in the world. Statistics are obtained from reliable sources for accuracy.

According to the report provided by the Islamic Corporation for the Development of the Private Sector (ICD), the growth trend of the gross assets of Islamic finance in 2019 is 2.880 billion with a growth rate of 14% amounted to US dollars. Islamic banks make up the majority of global Islamic financial assets. In 2019, this industry grew by 14% and amounted to 1.99 trillion US dollars. It should be noted that the growth of the gross assets of Islamic finance in the world by 2024 will reach 3,690 billion. It is expected to reach USD.

Islamic banks are widely regarded as financial institutions that prohibit usury and do not lend. Specifically, in theory, Islamic banks sell and buy goods and services at a profit margin. This definition may confuse Islamic banks with conventional banks. In fact, traditional banks lend money to the borrower to purchase goods and services. The Islamic financial system cannot deviate from the laws of the Islamic religion, and this is the main factor in its development and gaining respect. We will mention the emergence of Islamic finance based on the religion of Islam and aspects related to Islamic finance.

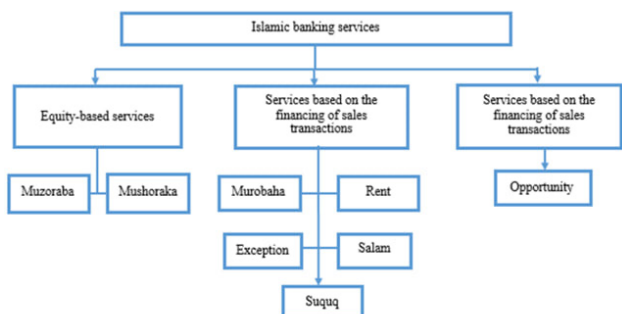


Figure 1. Types of Islamic banking services.

Islamic banks differ from conventional banks because they support interest-free loans. Islamic banks operate

on different principles and have different risk profiles. Islamic banks have two types of regulations; the first is the regulations set by the government and the central banks, and the second is the regulations set by the Sharia Supervisory Board, which approves the products of Islamic banks and supervises the implementation of the rules set by the council.

The Central Bank sets some rules specific to Islamic banks. For example, the minimum capital requirements for establishing an Islamic bank are higher than for conventional banks. Islamic banks have to pay more taxes and registration costs because it is an asset-based bank and the bank has to own the goods that it then sells, which is ultimately paid for by the customer, but this increases costs.

The economic performance of any country depends on its financial sector. The role of the banking sector is important in directing public funds to productive investments that lead to economic growth. Conventional banking is based on interest and is against Islamic principles. Islamic banks, on the other hand, are Sharia-compliant and operate on the basis of Islamic law. The Islamic financial system also includes a number of financial institutions, including commercial and investment banks and companies, insurance, e-commerce, and asset management companies.

According to the Islamic Finance Development Indicator-IFDI report published in 2023, the total assets of the Islamic financial system in 2015 were 2.170 trillion. If it is US dollars, by 2021 it will be 3.96 trillion. reached US dollars (that is, the aggregate average annual growth rate during this period was 10-12 percent. In 2021, Iran (1.235 trillion US dollars), Saudi Arabia (896 billion US dollars) and Malaysia (650 billion US dollars)) by owning 70% of Islamic finance assets (\$2.781 trillion), Tajikistan (84%), Burkina Faso (27%) and Ethiopia (26%) recorded the highest growth rates in this sector in 2021.

70 percent of the assets of the Islamic financial sector (2.765 trillion US dollars) are accounted for by 566 Islamic banks operating in 47 countries. This means that the banking network is a key factor in the growth of the Islamic finance sector. Of course, this process is mainly related to the opening of new Islamic financial institutions in various countries. For example, in the last few years, the Islamic financial system began to develop in the CIS countries. Kazakhstan, Kyrgyzstan, Azerbaijan and Tajikistan have introduced changes in their legislation and started the operation of Islamic banks.

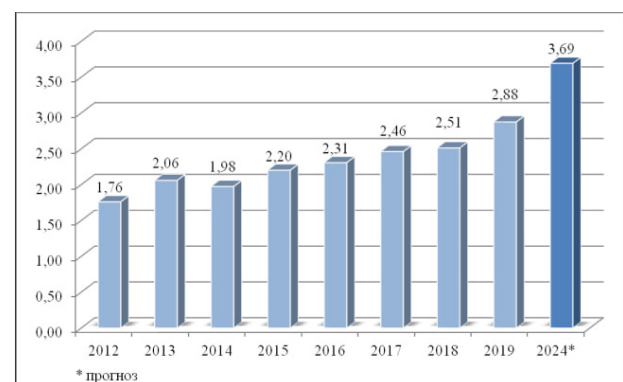


Figure 2. Changes in the capital of Islamic banks in the world in 2012-2024 (billion in US dollars).

The potential of the Islamic finance sector is assessed through the following five sectoral activities:

1. Islamic banks

2. Takaful (Islamic Insurance)
3. Other Islamic financial organizations (investment companies, microfinance institutions, etc.)
4. Sukuk (securities based on Islamic finance)
5. Islamic fund institutions.

The main goal of developing the world financial market, especially Islamic finance, is to stimulate production and improve people's lifestyles.

Conclusion. In summary, the Islamic finance industry has shown remarkable resilience against the challenges posed by the pandemic, and its total assets are expected to grow by 17% in 2021, approaching US\$4 trillion. The growth of the sector was evident in all its main branches, including Islamic banking, sukuk, Islamic funds and other Islamic financial institutions. It is worth noting that Islamic banking, the largest sector with a share of 70% of total Islamic financial assets, has achieved significant growth due to factors such as government support, operational efficiency and stable demand. That is, the net income of the sector increased significantly by 290%, while the average return on its assets also increased.

We make the following suggestions for future research:

- Since the introduction of Islamic finance in the financial system of the country is being carried out more familiarity with foreign literature and scientific articles in this direction;

- By strengthening cooperation relations with countries with well-developed Islamic banking, learning from their experience will help to avoid many mistakes and provide an opportunity to build the sector on a solid foundation from the beginning;

- The implementation of Islamic finance allows for the emergence of new financial products in the banking and financial institutions of the country in a short period of time, the opportunities to learn international/foreign experience in this field, the opportunities to reduce risks in the banking and finance sector, and the serious development of the industry as a whole.

- The introduction of Islamic financial mechanisms based on partnership, i.e. profit-loss sharing, or in other words, having a moral basis, will allow residents and entrepreneurs to offer alternative financial mechanisms, which will lead to the activation of their economic and financial activities.

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