THE CONCEPT AND ESSENCE OF ISLAMIC FINANCE IN THE WORLD

Sattarova Dilfuza Dilshodbekovna
Independent researcher, JSCB "Hamkorbank" Urgench branch, manager.

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Abstract. *The article discusses the concept and essence of Islamic finance, its main principles, Islamic banking and their difference from conventional banks. This study aims to explain the theoretical aspects of the most common financial methods of Islamic banking, the products of Islamic Capital Market, functioning and differences of Islamic insurance. In this article, we offer an overview to provide elementary information and serve as the basis for further study.*

Key words: *Islamic finance, Islamic banking, sukuk, takaful, Islamic Capital Market, mudarabah, musharakah, salam, murabaha, ijarah, istisna.*

DUNYODA ISLOMIY MOLIYA TUSHUNCHASI VA MOHIYATI

Annotatsiya. *Maqolada islom moliyasining mazmun va mohiyati, ularning asosiy tamoyillari, islom banklari va ularning an'anaviy banklardan farqi haqida so'z boradi. Ushbu tadqiqot islom bankining eng keng tarqalgan moliyaviy usullarining nazariy jihatlarini, islom kapital bozori mahsulotlari, islom sug'urtasining faoliyati va farqlarini tushuntirishga qaratilgan. Ushbu maqola orqali biz asosiy ma'lumotlarni taqdim etish va keyingi o'rganish uchun asos bo'lib xizmat qilish uchun umumiy nuqtai nazarni taqdim etamiz.*

Kalit so'zlar: *islom moliyasi, islom bank ishi, sukuk, takaful, islom kapital bozori, mudarabah, musharaka, salam, murabaha, ijara, istisna.*

КОНЦЕПЦИЯ И СУТЬ ИСЛАМСКИХ ФИНАНСОВ В МИРЕ

Аннотация. *В статье рассматриваются понятие и сущность исламских финансов, их основные принципы, исламский банкинг и их отличие от обычных банков. Это исследование направлено на объяснение теоретических аспектов наиболее распространенных финансовых методов исламского банкинга, продуктов исламского рынка капитала, функционирования и различий исламского страхования. В этой статье мы предлагаем обзор, чтобы предоставить элементарную информацию и послужить основой для дальнейшего изучения.*

Ключевые слова: *исламские финансы, исламский банкинг, сукук, такафул, исламский рынок капитала, мудараба, мушарака, салам, мурабаха, иджара, исключение.*

Introduction. Islam guides man in his relationship with God and gives him the norms which govern his temporal existence ,since Islam is concerned with the spiritual, political, social-economical, moral and all other material aspects of the human being. The fundamental role of the financial system in time and space is to provide the opportunity for the efficient allocation of financial and real resources competing for goals and objectives. A well-functioning financial system encourages investments by identifying and financing well business opportunities, stimulate savings, follow-up manager performance, makes trading possible, provides hedging from any kind of risk and diversification with different kind of assets, and eases the exchange of goods and services. These functions ultimately enable efficient allocation of resources, quick saving of physical and human capital, and faster technological advancements, which foster economic growth.[1]

Islamic finance refers to how businesses and individuals raise capital in accordance with Sharia, or Islamic law. It also refers to the types of investments that are permissible under this form of law. Islamic finance can be seen as a unique form of socially responsible investment. The most important feature that distinguishes this type of finance from traditional finance is that it does not contain interest. In Islamic finance, instead of paying interest to the holders, the payment of dividends and the fact that Islamic finance direct savings to real investments are the most fundamental differences between traditional finance and Islamic finance. It is important that transactions such as establishment, development, organization, management, service production and supply of all these tools in islamic finance are carried out in accordance with Islamic Law.[2]

Material and methods. It is only in the past few decades that efforts have been made to explain Islamic financial and economic principles and rules in modern analytical terms and, despite considerable published research, there is still some confusion in regard to applying a precise definition to various social sciences prefixed with the term “Islamic,” such as “Islamic economics” or “Islamic finance.” One of the main reasons for this confusion is the tendency to view different aspects of such a system in isolation, without looking at it in its totality. For example, the term “Islamic finance” is often deemed to denote a system that prohibits “interest.” However, this simple description is not only inaccurate but is itself a source of further confusion. Unfortunately, too, a number of writers have taken the liberty of expressing opinions on these issues without sufficient knowledge of Islam, its primary sources, its history and often without even a working knowledge of Arabic—the language of Islam.1 Against the backdrop of a politicized atmosphere, such attempts render an understanding of these issues even more difficult.

The economist Douglas North contends that what distinguishes one economic system from another is the “institutional scaffolding”—the collection of rules and norms along with their enforcement characteristics—in that system. He defi nes institutions as rules of behavior designed to impose constraints on human interaction. These institutions “structure human interaction by providing an incentive structure to guide human behavior. But an incentive structure requires a theory of the way the mind perceives the world and its functioning so that institutions provide those incentives” (North 2005: 66).

Islamic finance is a system that is based on Islamic principles and values. It eliminates *ribā* (interest) and ensures a financial system, which is *ḥalāl* (permissible). It is characterized by the absence of interest-based financial institutions and transactions, doubtful transactions or uncertainty (*gharar*), stocks of companies dealing in unlawful activities and unethical or immoral transactions such as market manipulation, insider trading and short-selling.[3]

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[1] Iqbal, Zamir and Mirakhor, Abbahals (2011), An introduction to Islamic finance. Theory and Practice(Second edition). John Wiley &Sons (Asia) Pte.Ltd. Singapore.

[2] Akten Curuk, Suna(2013).development of Islamic finance in Turkey, Current issues and Proposed Solutions. Selcuk University, Institute of Social Sciences(Unpublished master thesis),Konya.

[3] Öndeş, T., Ahmid, A. and Faraj, A. (2019), “*Financial performance of Islamic banks in Turkey and the United Kingdom: a comparative study*”, European Scientific Journal, Vol. 15 No. 4, pp. 87-104.

Islamic banking and finance research has received significant attention in recent years. Nevertheless, Narayan and Phan (2017) argue that research in this area is still evolving. Prior research on IB&F has focused mainly on investigating the performance of Islamic banks (e.g., Mobarek and Kalonov 2014; Saraç and Zeren 2015; Kabir et al. 2015; Mollah et al. 2017; Grira et al. 2016). Another stream of research has examined the corporate governance system of Islamic banks (Hayat and Hassan 2017; Elnahas et al. 2017; Jan et al. 2021). Previous studies have also explored the features of Islamic bond markets (Naifar and Hammoudeh 2016) and the Islamic Insurance system (Raza et al. 2019). Furthermore, research has explored some ethical issues related to IB&F. For instance, Al-Suhaibani and Naifar (2014) explore the ethical framework of Islamic financial institutions (IFIs) and Platonova et al. (2018) examine the social responsibility roles of IFIs. The evolution of research in a field of study induces scholars to quantitatively review its scientific production to understand its "intellectual structure" (Rivera and Pizam 2015). This helps develop a knowledge base for this field, identify its research trends, understand its theories and methodologies, determine the contributions and suggest potential avenues for future research (Ferreira et al. 2014). The bibliometric analysis is an innovative methodology aiming to reveal the development and structure and visualize the scientific production in a field of study (Mostafa 2020; Qi et al. 2018). It is applied to explore the knowledge structure in different fields of research, such as Halal food (Mostafa 2020), circular economy (Alnajem et al. 2021), operational research (Argoubi et al. 2020), innovation (Yahaya et al. 2020), and corporate governance (Zheng and Kouwenberg 2019)[4].

The theoretical and practical aspects of the organization of Islamic financing of projects and its effective management were discussed by major foreign economists M. Taqi Usmani, H. Visser, Rajesh K. Aggarwal, Tariq Yousef, Mohammad Jamal Haider, Gao Changchun, Lady Mahara Ginting, Nafisah Ruhana, Marizah Minhat, Nazam Dzolkarnaini, Mariatul Aida Jaffar, Rosidah Musa, Gait, A., & Worthington, A., Jalaluddin, A., Victoria Stoika , Christopher G. The scientific works of scholars such as V. Antropov, T. Gafurova, S. Mokina, O. Trofimova, I. A. Zaripov, I. Bekin, Y. Berdaulet from the CIS countries have reflected the issues related to Islamic securities and Islamic finance. In the scientific works of Uzbek researchers H.Khasanov, M.Sultanov and O.Davlatyarov, scientific researches in this field were carried out.

Discussion and Results. Islamic finance has emerged in a relatively short time in the area of international finance. The development of Islamic finance is divided into four periods(1 table).

1-table.

The history of the development of Islamic Finance.

Stages (years)	Classifications
Establishment period (1963-1976)	Intensive studies were conducted The development of international corporation and banking activities were ensured
Expansion time (1977-2002)	This period was strengthened by the sharp incease in oil prices and capital cumulation in the Middle East. More than 100 islamic banks were established around the world,such as Dar al-al Islam in 1981 and Al-Baraka in 1982

[4] Ahmed Hassanein, Mohamed M. Mostafa. Bibliometric network analysis of thirty years of islamic banking and finance scholarly research. Quality & Quantity https://doi.org/10.1007/s11135-022-01453-2

International recognition period (2003-2009)	Islamic finance is recognized globally by regulators around the world,particulary in China, Europe and The United States International banks have participated in Islamic finance operations,including Islamic product Among these banks ; there are more than 200 Islamic financial institutions in more than 70 countries, such as The Adaptation(USA),ANZ(Australia),ABNAmro(Netherlands), GoldmanSachs(USA),HSBC(England),Deutschebank(Germany),Societe Generalle(France), Saudi-American bank(USA-Saudia Arabia) and The Saudi –British bank(UK-Saudia Arabia).
Evaulation period (since 2009)	During this period ,the growth momentum of islamic financial assets sustained during the global finance crisis was recognized by many parties, including policy makers, bankers and economists, and contributed to the stability of financial markets.

Source: Author's work based on Tiby, Amr Mohamed eland Grais, Wafik. Islamic finance and Economic development-Risk Management, Regulation and Corporate Governance. 2015.John Wiley & Sons. Inc. New Jersey, USA.

The main purpose of Islamic finance is to promote economic and social welfare within the frame of Islamic Law by encouraging the principles of Islamic Law in the business world. The principles of sharing profit promotes banks to turn to operations that provide long-term earnings rather than short –term earnings. In this system,it is pioneered both banks and investors to cayyr out appropriate works before entering projects that protect their interests. Distributing of high returns to the shareholder bring welfare to the economy and maximize social benefits.

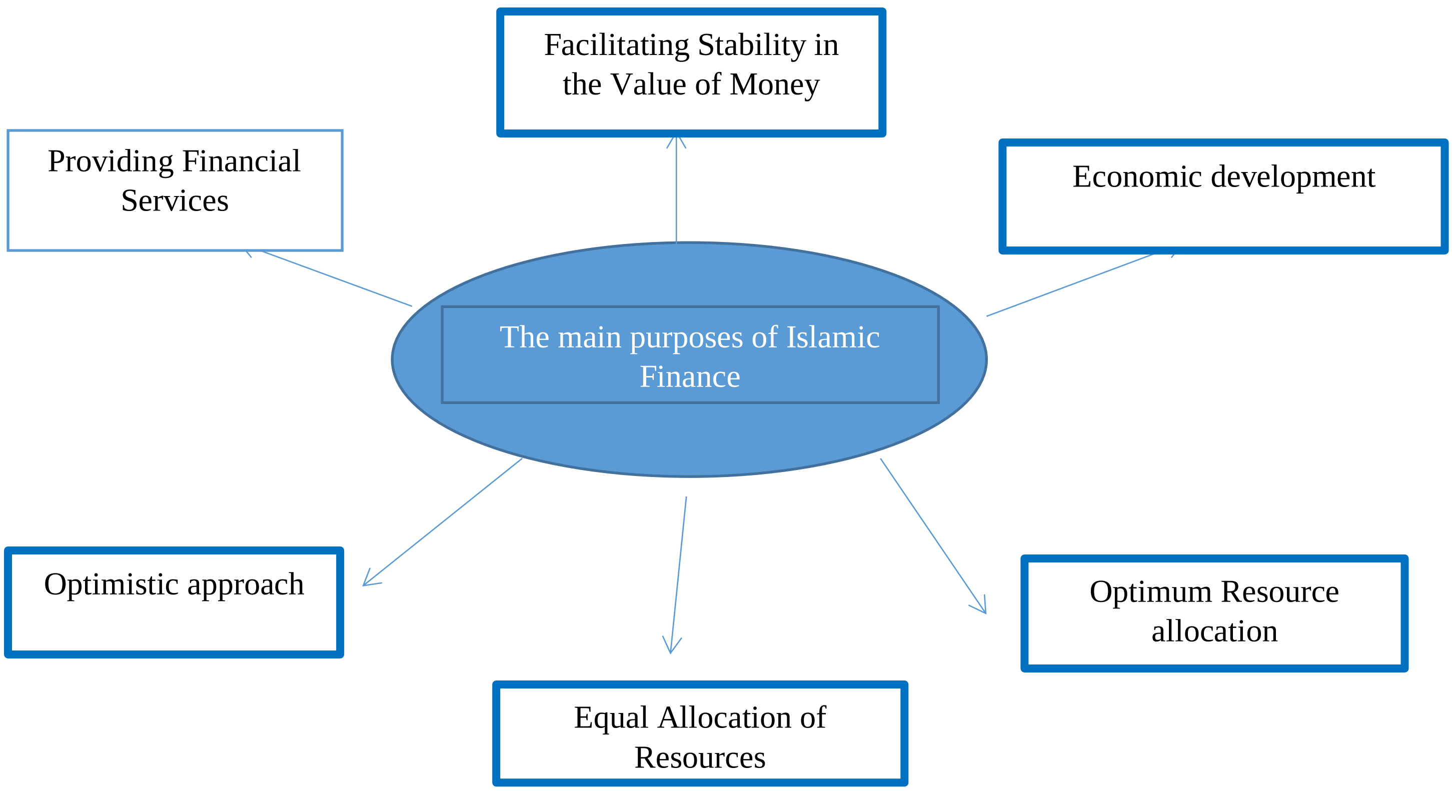

Figure 1. The main purpose of Islamic Finance. Source: Author's work based on Alam, Nafis,Gupta,Lokesh and Shanmugam,Bala. Islamic Finance: A practical Perspective.2017. Palgrave Macmillian publishing ,Cham, Switzerland.

The most known characteristic of Islamic finance is justice ,with loss and gain sharing and the ban of interest. The fundamental principles of Islamic finance are shown in the

Table 2.

The fundamental principles of Islamic finance.

Principles	Meanings
Prohibition of Interest	Literally means "surplus" and is termed "any adjust capital increase, whether in loans or sales"; The aim of this principle is to develop an environment based on justice.
Risk sharing	Fund suppliers are being investors instead of being creditors; The financial capital supplier and the entrepreneur undertake equally business risks in exchange for dividends.
Money as "Potential Capital"	Money is accepted only a means of exchange in Islam; When integrated with other resources to lay on productive activity, it becomes real capital; The time value of money is accepted as capital by Islamic finance, when it acts as capital; Stacking of money is considered forbidden; As long as it use for correct product and service ,money is considered as purchasing power in Islamic finance.
Prohibition of Uncertainty	Excessive uncertainty (Gharar) and gambling (Maysir) are inappropriate; Derivates such as options, forward and futures are considered as non-Islamic; Islamic Finance Institutions do not participation bargaining where the results are unclear; If these elements are eliminated ,the current stock exchange transactions are called Islamic Stock Exchange or Indicates.
Sanctity of Contract	Islamic Finance considers adherence to the contract as sacred duty; In commercial activities taking religious sensitivities into account ,the procedures are based on four basic principles: -Sales; in return for a return of ownership of property, -Rent; in return for the right to use the property, -Grant(Gift);unrequited transfer of ownership

	and , -Loans; transfer of the right of use of the property for free.
Islamic Law Approved Activities	Investing in business dealing with gambling ,alcohol, casino and so on are forbidden in Islamic finance; Institutions are expected to constitute an Islamic Supervisory Committee consisting of Independent Islamic Law auditors and Islamic Lawyers who act as a consultants to banks.

Source: Author's work based on Askari, Hossein, Iqbal, Zamir, Mirakhor, Abbos. Globolization of Islamic finance: Convergence, Prospects and Chellenges.2010. John Wiley & Sons. Inc. Singapore.

Islamic Finance Industry can be basically divided into three main markets: Islamic Banking, Islamic Capital Markets and Islamic Insurance. The principle component and pioneer of the sector is Islamic Banking . It is defined by OIC (Organization of Islamic Conference) as "Islamic Bank is a financial Institution, whose statutes, rules and procedures expressly state its Commitment to the Principles of Islamic Shariah and to the banning of the receipt and payment of interest on any of its operation". The difference between Islamic and conventional banks are shown in the table 3.

Table 3.

The difference between Islamic and conventional banks.

Conventional banking	Islamic Banking
Money is a commodity besides medium of exchange and store of value.	Money is not a commodity though it is used as a medium of exchange and store of value.
Time value is the basis for charging interest on capital	Profit on trade of goods for charging on providing service is the basis for earning profit
Interest is charged even in case the organization suffers losses by using bank's fund	Islamic bank operates on the basis of profit and loss sharing
While disbursing cash finance, running finance or working capital, no agreement for exchange goods and services is made	The execution of agreements for goods and services is a must while disbursing funds under Murabaha, salam and istisna contracts.
Commercial banks use money as a commodity which leads to inflation	Islamic banks tends to create a link with the real sector of the economic system by using trade related activities
The investor is assured of a predetermined rate of interest	In contract it promotes risk sharing between provider of capital(investor) and the user of funds(enterpreeneur)
Lending money and getting it back with compound interest is the fundamental functions of the conventional banks	Compounding calculations is strictly prohibited under Islamic banking system
It can charge additional money in case of defaulters	The Islamic banks have no provision to charge any extra money from the defaulters
Conventional banks invest their deposit in interest based modes	Islamic banks only deals in Halal products and services, all transactions must be in Shariah Compliance
The status of conventional bank, in relations to	The status of Islamic banks in relation to its

its clients, is that of creditors and debtors.	clients is that of Partners, Investors, Trader, Buyer and Seller
A conventional bank has to guarantee of all its deposits	Islamic banks cannot guarantee of all its deposits

Source: Crus, Alcoba, Martinez, Raul and Jimmenez Avial. Islamic Markets. 2012.www.slideshare.net/alco700l/Islamic-markets.

Islamic banks utilize two classes of transaction models to accomplish a banking solutions. These financial models are 1) Profit and loss –sharing (PLS), also called participatory modes,i.e, musharakah,and mudarabah 2) purchase and hire of goods or assets and services on a fixed-return basis ,i.e., murabaha, salam, istisna'a, and leasing(Ijarah) .

Mudarabah. Mudarabah alludes to a type of business contract in which one party brings capital and the other work experience and individual effort. The financier is known as "rabal maal" and the entrepreneur as "mudarib".the proportionate share in profit is determined by mutual agreement. Loss is borne by the capital owner, in which case the entrepreneur gets nothing for his labor. However, the entrepreneur may be liable for compensation if he/she acts in contradiction with the intend, defect and contract condition.

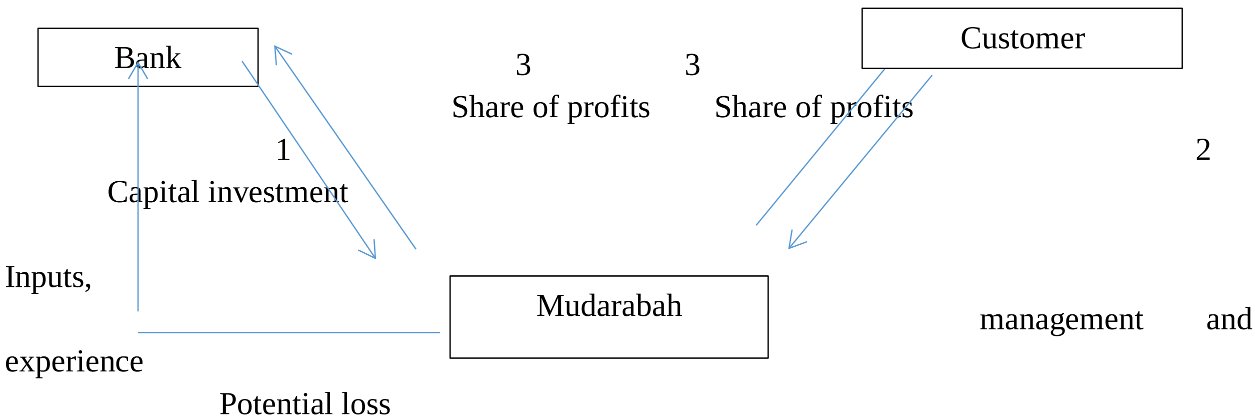

Figure 2. Mudarabah transaction model. Source: Erdi Bayram, U.X.Gozkonan. S.Baha Yildiz. Financial management .Islamic Finance.Chapter16.A to Z Islamic banking. Citi research(2018).

Mushorakah. It is a profit and loss-sharing method in which both parties participate in the capital. In this partnership, profit is shared according to the agreement; however the loss is distributed according to the share in the capital.

Murabaha. The cost of the goods is notified to the customer and sold with the addition of profit. In other words, the customer knows how much profit he gives to the seller because of goods he buys. Mostly it operates in the form of profitable futures sales of free purchased goods. During the purchase of goods from the seller on behalf of the bank, the bank customer represents the bank by proxy.

Salam. In salam method, the money is paid in advance and the goods are delivered in the future. Size of the goods sold, weighing, varieties and so on. All qualities should be determined in a such way that there are no unknown direction; also the term of delivery of the goods should be known. The price of the goods must be delivered to the seller at the time of the sale contract.

Istisna'a. Islamic banks to buy a project (on behalf of the purchaser) that is under construction and will be completed and delivered on a future date.

Ijarah. Ijarah refers to a lease or commission contract that comprises an interchange of right of use or advantage of an asset or a service for rent or commission for an agreed period. In the context of Islamic finance, the ijarah concept is usually applicable in financing contracts such as in real property financing, vehicle financing, project financing and personal financing.

Islam Capital Market can be defined as securities markets where all kind of trading and other operations are carried out according to Islamic principles and requirements. Among the products currently available for which Shariah principles are applied include (Table 4):

Table 4.

Islam Capital Market products.

Islamic capital marker products	Definition
Sukuk	Sukuk is the securitization and sale of a commercial asset through certificates. Those who receive these certificates will share this asset in proportion to the certificates they have. Therefore, he income of the said asset belongs to them.
Shariah-Compliant Stock	Islamic stocks are a subset of conventional stocks, and these stocks pass through two steps of screening ,namely, qualitative and quantitative screening , to be Shariah compliant. A qualitative screening process excludes stocks issued by firms those core business activities are not in line with Shariah, such as conventional banks and other finance companies, winery, brewery and weapon products. In addition , a stock needs to meet a certain financial ratio requirements in order to pass a quantitative screening process. For example, The debt ratio cannot be more than 30%.
Islamic Unit Trust Funds	These funds are a collective investment scheme that offers investors tha opportunity to invest in a diversified portfolio of Shariah-compliant securities, fixed income securities and money market instruments.
Islamic Real Estate Investment Trusts	I-REITs are partnerships which have to comprise at least 50% of the assets from real estate and invest in areas that comply with Islamic principles.
Takaful (Islamic Insurance)	Takaful refers to the insurance service carried out on the basis of risk-sharing under the management of aspecialist company organized in accordance with Shariah. This business model ,also called participation insurance ,was first tried in 1979 in Sudan. Takaful companies spread to Malaysia in 1985 and then to European countries.

Source: Erdi Bayram,U.X.Gozkonan,S.Baha Yildiz. Financial management .Islamic Finance.Chapter16.A to Z Islamic banking. Citi research (2018).

Conclusion. There is no doubt that the Islamic finance sector has felt the repercussions of the financial crisis, but on the whole it has weathered the storm better than conventional finance and its prospects remain high. Governments are in a position to give a direct impetus to this recovery through their involvement in the Sukuk market. If Islamic finance is to compete with mainstream global finance, the industry needs to improve transparency and foster credibility by harmonising standards and practices, not least, the variety of Shari'ah interpretation between regions and at times between institutions. Regulatory oversight needs to be sharpened as well. These measures could be critical in broadening the appeal of Islamic finance and strengthening the credibility of the Islamic system as a sustainable alternative the mainstream financial system. The Islamic finance industry also needs to work on innovation. Shari'ah compliant products can be more complex than mainstream ones because every transaction is based on a trading agreement. Many sustainable equivalents to mainstream financial instruments are still lacking, including corporate treasury and derivative products. At the same time, innovation is hampered by the limited number of Shari'ah board members (Shari'ah scholars) able to vet financial products for Shari'ah compliance. Finally there is a huge shortage of suitable skilled employees working within the industry. This scarcity of suitably qualified human capital can only be redressed by increasing awareness of the career possibilities within the industry and by the offering of globally accepted qualifications.

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