

ISLAMIC FINTECH INSTRUMENTS: NEW OPPORTUNITIES FOR DIGITAL ECONOMY OF UZBEKISTAN

Sirojiddin Abrorov

Tashkent State University of Economics,
s.abrorov@tsue.uz, ORCID 0000-0001-9559-0231

Jahongir Imamnazarov

Tashkent State University of Economics
jakhongir.imamnazarov@gmail.com

ABSTRACT

The Islamic financial system is one of the fastest-growing systems in the world, which is actively strengthening and expanding its position internationally. This is evidenced by the rapid growth in the number of Islamic financial institutions, the opening of Islamic windows and branches by traditional banks, as well as the growth in sales of Islamic securities on leading stock exchanges. The global financial and economic crisis of 2008 and the global financial crisis caused by the COVID-19 pandemic made it an urgent task to use and expand Islamic financial mechanisms that rely on the real sector and contribute to the development of society. This article analyzes the growth of the Islamic financial sector, particularly Sukuk - Islamic securities in the global financial market and the current state of Islamic finance in Uzbekistan. Also presented are the results of the, including a survey on the introduction and development of Islamic finance in Uzbekistan.

CCS CONCEPTS

• Islamic finance; • sukuk; • issue; • real economy; • financial market; • digital economy;

ACM Reference Format:

Sirojiddin Abrorov and Jahongir Imamnazarov. 2021. ISLAMIC FINTECH INSTRUMENTS: NEW OPPORTUNITIES FOR DIGITAL ECONOMY OF UZBEKISTAN. In *The 5th International Conference on Future Networks and Distributed Systems (ICFNDS 2021)*, December 15, 16, 2021, Dubai, United Arab Emirates. ACM, New York, NY, USA, 5 pages. <https://doi.org/10.1145/3508072.3508203>

1 INTRODUCTION

The negative impact of the COVID-19 pandemic on the global economy is still being felt. Governments are taking steps to transform the financial sector to maintain economic stability. In particular, in 2021 Uzbekistan plans to issue sukuk-Islamic securities on a trial basis. It is planned to attract local and international investors, develop the financial market and accelerate the reform process [1]. In addition, starting this year, several commercial banks intend to launch the Islamic Window services. It is known from world experience that these processes are the first stages of the introduction of Islamic finance.

Permission to make digital or hard copies of all or part of this work for personal or classroom use is granted without fee provided that copies are not made or distributed for profit or commercial advantage and that copies bear this notice and the full citation on the first page. Copyrights for components of this work owned by others than ACM must be honored. Abstracting with credit is permitted. To copy otherwise, or republish, to post on servers or to redistribute to lists, requires prior specific permission and/or a fee. Request permissions from permissions@acm.org.

ICFNDS 2021, December 15, 16, 2021, Dubai, United Arab Emirates

© 2021 Association for Computing Machinery.

ACM ISBN 978-1-4503-8734-7/21/12... \$15.00

<https://doi.org/10.1145/3508072.3508203>

It is known that one of the main goals of Islamic finance is to influence the real sector of the economy and ensure its growth. Of course, it is also useful for customers who do not use banking services in the country. Today, Uzbekistan, which has strong Islamic spiritual roots, may be one of the most promising countries for Islamic finance in Central Asia. As an alternative and innovative method of financing, it is necessary to analyze the state and prospects for the development of Islamic banking and financial services, including the sukuk market, in the international financial market, and if this system is used in our country, then its impact on the economy should be assessed.

If we look at the history of Islamic finance, we will see, they began form at the end of the sixth century. The modern history of Islamic finance, which has spread as a single system in the Middle East, North Africa and Central Asia since the 7th century, began to take shape in the 1950s as a new system that we know.

After the independence of the Muslim-majority countries in the second half of the last century (UAE 1971, Algeria 1962, Kuwait 1961, Malaysia 1957, Sudan 1956, Pakistan 1947), large deposits of oil and gas were discovered in these countries, they began to mine on a large scale, and the volume of exports of these products increased. In turn, the rise in oil prices on world markets has led to the formation of large reserves in these countries. However, problems have arisen with the fact that the accumulation of savings using traditional banking and financial products does not meet the requirements of Muslim-majority communities. This required the formation of a financial system based on the principles of Islam.

The first financial institution in accordance with Islamic principles, Mit Ghamr Savings Bank, was established in 1963 in Egypt. This fund has demonstrated in practice that Islamic finance can function as an alternative financial system. The creation of the Islamic Development Bank in 1975 announced to the world community that Islamic finance had entered the global arena. Since then, the number of Islamic financial institutions has increased and their geographic coverage has increased.

While Islamic financial products were rapidly introduced and developed all over the world in the second half of the twentieth century, in the twenty-first century Islamic finance is subject to financial crises, fair distribution of risks, reliance on real assets and expensive services for the economy. Islamic financial services and products, especially sukuk, are also widely used in developed countries where Muslims are sparsely populated.

Research shows that although the share of Islamic finance in the global financial structure is small, their growth rates are high and their efficiency is much higher.

2 RELATED WORK

Among the scientists of the CIS countries are V.Antropov [2], T.Gafurova [3], S.Mokina [4], O.Trofimova [5], I.A. Zaripov [6],

I.Bekkin [7]. Their work reflects the issues of Islamic securities and Islamic finance.

Researchers in the field of Uzbek researchers X. Khasanova [8], [9], M.Sultanova [10] and O. Davlatyarova [9] also conducted research in this area, and this work continues today. Also B.Juraev [11] [12] [13] translated from Russian into Uzbek some literature on Islamic finance. These scientific works are based on the theoretical foundations of Islamic finance and the activities of Islamic financial institutions, and sukuk has not been studied on a scientific basis.

Although the number of scientific research related to sukuk is growing, it is relatively small compared to other fields. For this reason, it is very important today to conduct a study on the introduction of sukuk in Uzbekistan in order to increase the activity of the stock market and attract public funds.

Ibrahim and Minai studied the importance of sukuk to attract investment in enterprises [15]. The results show that it is worthwhile for enterprises with smaller and higher investment potential to issue sukuk. It is also inevitable that the government's support for the sukuk market will give a positive result.

There is little scientific research on the impact of sukuk on the economy, and the first attempt has been made to study the impact of sukuk issuance on GDP, gross fixed capital growth and trade. [18]. This article examines the impact of sukuk issuance on GDP, fixed capital growth and trade processes in 2005-2012. And it was found that sukuk issuance have a positive effect on GDP when all the issuing countries combined. Although the studies did not yield the expected results, they are important because they have taken a new direction. It is noteworthy that subsequent research in this area has led to significant results [19]. The work differs from the previous one in other factors and the choice of style. The influence of sukuk on the economic development of sukuk-issuing countries in 2000-2015 was studied. As a result, sukuk support economic growth in the long term. Corporate and state sukuk play an equal role in this.

3 RESEARCH METHODOLOGY

The article uses scientific abstraction, empirical, descriptive statistics, expert assessment, grouping, dynamic analysis, survey methods.

4 ANALYSIS AND DISCUSSION

The article uses scientific abstraction, empirical, descriptive statistics, expert assessment, grouping, dynamic analysis, survey methods.

Sukuk began to develop rapidly only in the 21st century, and there has been some growth over the past 20 years. In 2001, the annual budget was \$1.2 billion. By the end of 2020, the total volume of sukuk issued during the year amounted to 174.6 billion US dollars. It reached the US dollar (Figure 1). It should be noted that 2020 was the year when the most sukuk was produced. In total, by 2021, there will be about 1.4 trillion in the world. More than 1 million US dollars were issued. These data indicate that over the past period, large investments have been made in the issue of sukuk every year. Although the growth rates vary, the realization of annual issuance means that there is a stable demand for sukuk.

By the end of the year 2020, sukuk was issued in 27 currencies, including Malaysian ringgit, which amounted to 50,5 percent share or 719,2 billion. He was a leader with a value equal to the US dollar (figure 2). In the currency sector, the US dollar fell by 22.5% (320,3 billion.) and Saudi Arabia riyoli 7.7% (109.3 billion. US dollar) with a share of the top three. Also, Indonesian rupees (7,3 %, 103,8 billion. US dollar) and Turkish lira (3,4 %, 49 billion. US dollar) is one of the most issued currencies in terms of value.

In addition to the US dollar, the UK pound, which is considered to be one of the internationally recognized currencies, was also issued sukuk in the euro and Chinese yuan, totaling 326,6 billion. Equivalent to the US dollar (23%). It is noteworthy that this value is less than the international sukuk value. This means that international sukuk is also issued in local currency.

5 SURVEY.

Before making any proposals on implementation of Islamic finance in the country, a survey was conducted among certain groups, as it is very important to study the views of entrepreneurs, banks and the public on this issue [24].

The main objective of the survey was to study how the population and entrepreneurs are able to meet their financial needs through existing banking and financial institutions, what obstacles they face in this process (formal and informal), as well as their demand for Islamic financial services, institutions and their financial products.

Also, the survey attempts to explore the opportunities and to propose the necessary steps and procedures towards implementing an Islamic banking-financial system in the Republic of Uzbekistan.

5.1 Demographic information of the respondents

The survey consisted the 5 parts and included demographic information about the respondents, information on access to finance, availability of opportunities for Islamic finance, insurance market, as well as information on Islamic social finance.

The survey was conducted among business representatives, banks and individuals.

1. Business representatives / entrepreneurs

The survey was conducted in the form of direct conversations between 1,000 (one thousand) entrepreneurs / business representatives, and another 1,235 surveys were conducted online, using the Google form and Survey Monkey software. Thus, a total of 2235 entrepreneurs (business representatives) were surveyed.

2. Banks

Official letters were sent to all commercial banks in the country (30) with the application form attached, and response letters (along with completed questionnaires) were received from 27 banks.

3. Individuals

The survey was conducted online using the Google form and Survey Monkey software. A total of 4938 respondents took part in the survey.

47 percent of individual respondents were aged 31-45 years, while 44 percent were aged 18-30 years. 42 percent had higher education while 36 percent had only secondary school degree. Lastly, 25 percent of individual respondents were state employed, while 21 percent privately employed.

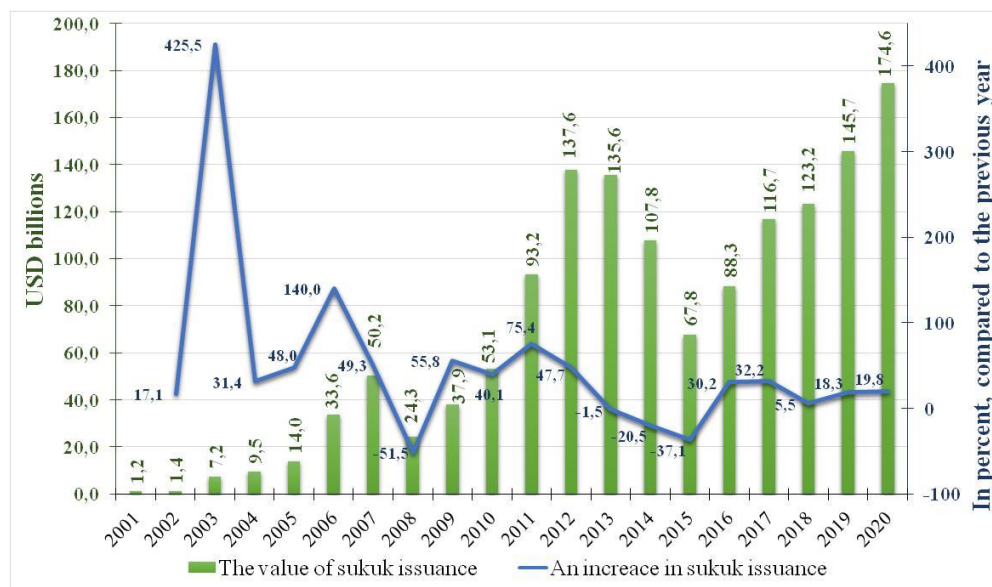


Figure 1: Dynamics of the volume of sukuk issuance in the world [22]

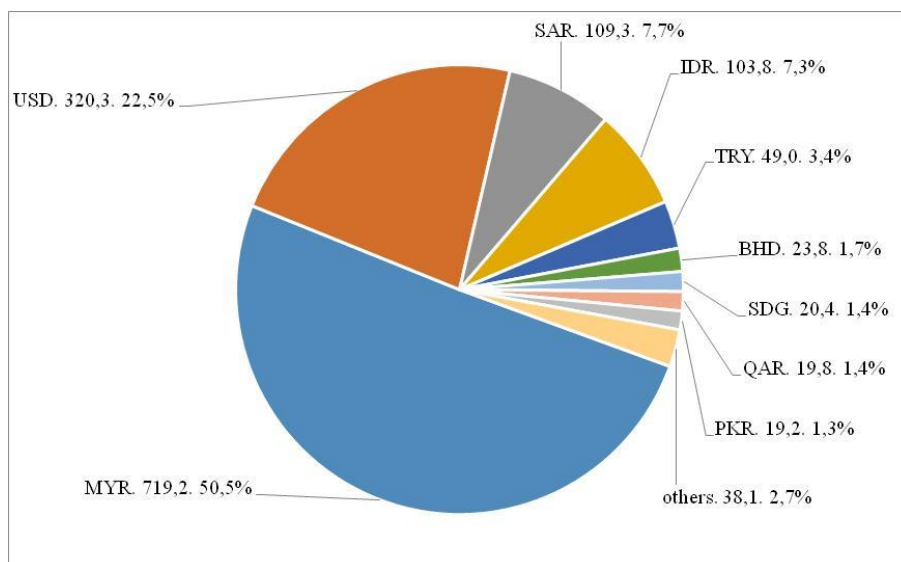


Figure 2: The volume of sukuk issuance in the cross-section of world currencies, 2001-2019 years (billion. US dollars) [22]

The organizational form of business of entrepreneurs participating in the survey is as follows:

- limited liability companies 44%;
- private companies 18%;
- individual entrepreneurs 16.5%.
- 64% of the abovementioned respondents are small companies, 25% micro firms, and 10% large companies.
- 26% of these companies were involved in industrial sector, 17% - in services, 22% - in trade, and 13% - in construction.

The annual gross income of 41% of these companies was less than 100 million UZS, 37% of them made between 100 million to 1 billion UZS, and only 4% made more than 10 billion UZS.

As regard the banks:

20 banks are joint-stock commercial banks, 5 privately owned, 2 are with foreign participation, and 2 are state-owned banks.

Businesses and Individuals: both individuals and businesses were asked if they had bank loans. 40 percent of businesses and 31 percent of individuals used formal channels for acquiring loans. The main purpose of acquiring a loan among businesses was to purchase equipment, vehicle, or special machinery (50 percent),

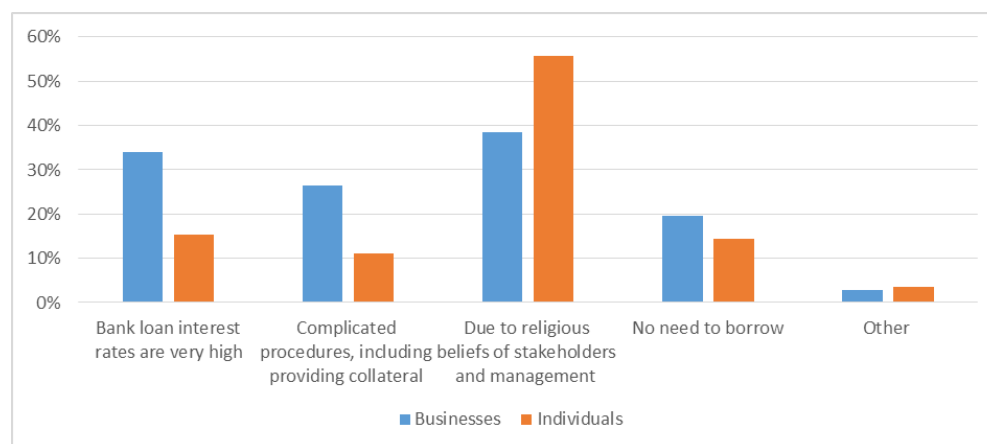


Figure 3: Reasons for not borrowing through formal channels

working capital and trade (34 percent), and agricultural projects (11 percent). Among individuals who received a bank loan, 53 percent of individuals took consumer loans and 28 percent mortgage loans. 60 percent of businesses and 68 percent individuals confirmed that they are not using bank loans.

5.2 Results of survey

The main concern for businesses and individuals was non-compliance of conventional loans with the Islamic norms. In particular, 38% of businesses and 55% of individuals answered that they did not use traditional loans because of their religious beliefs (Figure 3). This led them to discontinue and close lines of credit despite the business need. Other specific reasons include high-interest rates, complicated terms and conditions, and the reluctance of banks in giving loans.

Both individuals and businesses were asked about the difficulty of getting a bank loan and affordability of the interest rates charged by banks. 45 percent of individuals stated that receiving a banking loan is not too difficult but interest rate on loans is high (44 percent of individuals). Similarly, 42 percent businesses are also of the opinion that receiving loans from banks is not difficult but interest rate is high (36 percent of businesses). Additionally, 44 percent of businesses stated that conditions to get bank loans are not too difficult while 24 percent of them said the conditions are difficult due to collateral and covenants.

Banks: the degree of competition among banks was rated very high by 15 percent (4 banks) and high by 70.37 percent (19 banks). Competition with non-banking institutions was ranked not high by 85.19 percent (23 banks) and as high by only 7.41 percent (2 banks). Banks were also asked if they offered leasing services or not. During 2017-2018, 80 percent of banks offered leasing services, which dropped to 76 percent by 2019, while 6 banks (24 percent) did not offer any leasing services.

61 percent of businesses and 75 percent of individuals expressed their willingness to opt for Islamic Financial institutions when they convene operations in Uzbekistan. In contrast, 35 percent businesses and 22 percent individuals stated that their preference in choosing a particular institution would depend on the cost and

quality of services offered by Islamic financial institutions, whereas only 3 percent of the individuals stated that they would not be interested in services offered by Islamic financial institutions due to lack of knowledge and awareness. 47 percent of businesses and 55 percent individuals have expressed that they would not be much concerned even if Islamic financial instruments are highly-priced as primary concern is to comply with Islamic principles in their financial matters. On the contrary, only 22 percent businesses and 19 percent individuals hold contradictory views as the high cost of Islamic financial instruments would be their primary concern.

Furthermore, in case of implementation of Islamic Finance in Uzbekistan, 44 percent of businesses and 42 percent individuals stated that they would direct their funds for savings or partnership with Islamic banks, while 26 percent businesses and 36 percent individuals would rather not do so.

The individuals were asked: "How much would you invest in a profitable deposit or partnership agreement based on Islamic principles?" 26.3% of individuals are from 1 million to 5 million. UZS, and 23.7% expressed readiness to deposit (empty) funds in excess of 20 mln. UZS as deposits in Islamic banks (Figure 4).

6 CONCLUSION

The conclusion drawn from the experience of dualistic countries that have introduced Islamic financial instruments and products is that Islamic finance brings economic growth and efficiency to society, competing on an equal footing with the traditional financial system. The analysis shows that the increase in issuance of sukuk, an instrument of Islamic financing, has a positive effect on economic growth. In our opinion, sukuk issuance have a positive impact on the economy due to the following factors: Firstly, Muslims who cannot invest in traditional bonds are attracted to the economy due to the presence of factors such as usury and maysir from the point of view of Sharia. vision. Secondly, it is a convenient tool for reducing the level of risks by diversifying the investment portfolio. Thirdly, the principle of risk sharing encourages the issuer of sukuk to implement more investment projects. Fourth, the development of the stock market will increase competition among financial sector participants.

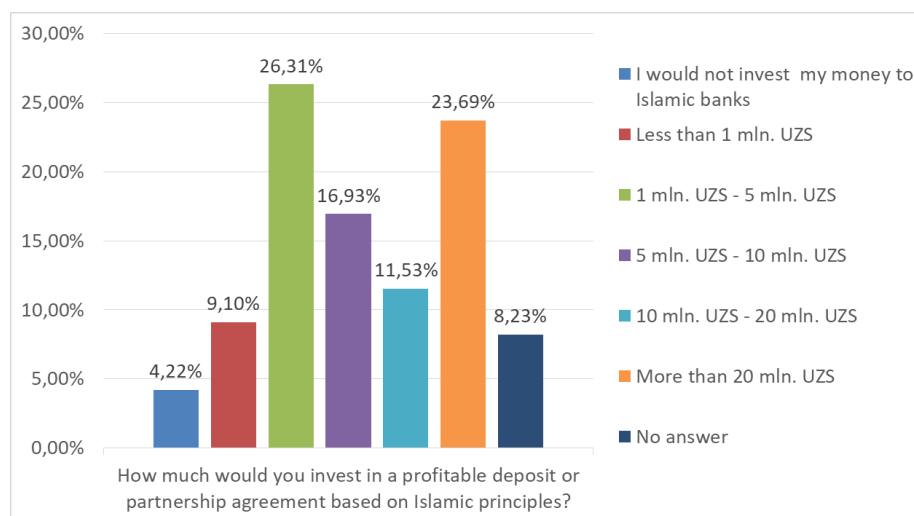


Figure 4: Funds that can be directed to Islamic banks deposits (in UZS)

Our hypothesis about the high need for Islamic finance, since the majority of the population of Uzbekistan professes Islam, was confirmed by the results of the survey. The conclusion from the entire analysis is that the introduction of Islamic finance will serve as a new factor in the development of the digital economy of Uzbekistan.

REFERENCES

- [1] Отабек Назиров, Капитал бозорни ривожлантириш агентлиги директори Отабек Назиров, Капитал бозорни ривожлантириш агентлиги директори. <https://kun.uz/news/2020/11/29/sukuk-ozbekiston-bozoridagi-yangi-moliyaviy-instrument-otabek-nazirov-bilan-suhbat>
- [2] Антропов В.В. Исламские финансы в глобальной экономике: современные тенденции и перспективы. Причины появления исламских финансов // Экономический журнал. 2017. №48.с. 57-77;
- [3] Гафурова Г.Т. Сукук в системе исламского финансирования // Вестник АГТУ. Экономика. 2011. №2. с. 90-94;
- [4] Мокина Л.С. Исламские ценные бумаги как источник финансирования инвестиционных проектов и перспективы их размещения на финансовом рынке России // Российское предпринимательство. 2017. Том 18. №22. с. 3429-3446;
- [5] Трофимова О. Мусульмане и ислам в Западной Европе // Мировая экономика и международные отношения. 2009. №10. с. 52-62;
- [6] Зарипов И.А. Малайзия – флагман исламских финансов // Вестник финансового университета. 2016. №4. с. 118-129;
- [7] Р.И.Беккин. Исламская экономическая модель и современность. – 2-е изд., перераб. и доп. – М.: Изд. дом Марджани, 2010. – 367 с.
- [8] Хасанов Х. Ахлокий (исломий) молиялаштириш тизими – инновацион молиялаштириш востиси сифатида (Ўзбекистон ва МДХ мисолида). “Иқтисодиёт ва инновацион технологиялар” илмий электрон журнали. № 5, 2017 й.;
- [9] Хасанов Х., Давлатяров О. Фоиз ставкаси ва инфляция даражаси ўртасидаги боғлиқликнинг исломий молиялаштириш жихатидан таҳлили. Стратегическое планирование – важный фактор стабильности устойчивого социально-экономического развития страны и регионов: материалы Форума экономистов/под общей редакцией. Т.Ахмедова.–Ташкент: IFMR, 2019. cc. 245-252.
- [10] Султанов М. Ўзбекистонда инвестиция фондларини ривожлантириш истикболлари. Иқтисодиёт фанлари бўйича фалсафа доктори (PhD) автореферати. -Т.: ТДИУ, 2019. 58 б.;
- [11] Жўраев Б. Ислоий молиялар ва банк тизими. – Т.: О'zbekiston, 2014. – 464 б.;
- [12] Жўраев Б. Ислоий молия асослари Матн / Е.А.Байдаулет. – Тошкент: «O'zbekiston» НМИУ, 2019. – 432 б.;
- [13] Жўраев Б. Ислои иқтисодий модели ва замон Матн / Р.И.Беккин – Тошкент: «O'zbekiston» НМИУ, 2019. – 360 б.
- [14] Zulkhibri M. (2015). A synthesis of theoretical and empirical research on sukuk. *Borsa Istanbul Review*, 15, p. 240. doi: 10.1016/j.bir.2015.10.001
- [15] Ibrahim, Y., & Minai, M. S. (2009). Islamic bonds and the wealth effects: evidence from Malaysia. *Investment Management and Financial Innovations*, 6(1), pp. 184–191. [Retrieved from]
- [16] Ahmad N., Daud S.N., & Kefelia Z. (2012). Economic forces and the sukuk market. *Procedia: Social and Behavioral Sciences*, 65, pp. 127–133. doi: 10.1016/j.sbspro.2012.11.101
- [17] Said A., & Grassa R. (2013). The determinants of sukuk market development: does macroeconomic factors influence the construction of certain structure of sukuk? *Journal of Applied Finance and Banking*, 3(5), pp. 251–267. [Retrieved from]
- [18] Echchabi A., Abd.aziz H., Idriss U., 2016. Does sukuk financing promote economic growth? An emphasis on the major issuing countries. *Turk. J. Islam. Econ.* 3, pp. 63–73. doi: 10.15238/tujise.2016.3.2.63-73
- [19] Smaoui H., & Nechi S. (2017). Does sukuk market development spur economic growth? *Research in International Business and Finance*, 41, pp. 136-147. doi: 10.15238/tujise.2016.3.2.63-73
- [20] Islamic Finance Development Report 2020: Progressing through adversity. The Islamic Corporation for the Development of the Private Sector and Refinitiv. p72.
- [21] Abrorov, S. (2019). The importance of sukuk in the development of economy: as an example of its impact on the income of the malaysian population. *Journal of Advanced Research in Dynamical and Control Systems*, 11(7), 927-931.
- [22] IIFM Sukuk report: A comprehensive study of the global sukuk market. *International Islamic Financial Market*, July 2021, 10th edition. p218.
- [23] Abrorov, S. (2020). The importance of sukuk in the development of economy: as an example of its impact on the income of the malaysian population. *Journal of Critical Reviews*, 7(2), 776-780. doi: 10.31838/jcr.07.02.142
- [24] <https://www.uz.undp.org/content/uzbekistan/en/home/library/poverty/landscaping-analysis-of-islamic-finance-instruments-in-uzbekista.html>