



PROSPECTS OF THE APPLICATION OF THE ISLAMIC FINANCIAL SYSTEM IN THE ACTIVITY OF UZBEKISTAN BANKS

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Abstract:

In the article isdiscussed the ways of Islamic financial instruments usingin commercial banks, as well analysis of its advantages and prospects for development. The article also presents the existing problems in the Islamic financial instruments in the activities of commercial banks of the Republic of Uzbekistan, as well as the author's approaches and proposals for their solution and prospects for theseimplementation development.

Keywords: Commercial banks, isiamic finance, musharakah, sukuk, mudoraba, murababaha, financing, Islamic banks, isiamic windows

INTRODUCTION

Islamic finance has shown a general growth trend in recent years. The emergence of the Islamic banking system in Egypt in the 1960s was not a huge event at the time, but for more than half a century, this industry has been developing steadily. In recent years, the concept of the Islamic financial system has taken a firm place in the agenda of financiers of many countries. In various countries, even in non-Islamic countries, including the United States and Great Britain, this financial institution operates as an alternative financing system to traditional banking services. Therefore, the study of Islamic banking is an urgent topic in the global economy.

With an annual growth rate of 15-20 percent, the Islamic bank has expanded its operations worldwide and today has its institutions in more than 75 countries.

The Republic of Uzbekistan became a member of the Islamic Development Bank (IDB) in 2003. During this short-term cooperation, ITB Group's portfolio in Uzbekistan has grown significantly, largely due to active cooperation with the Government. This was reflected in the approval of the financing of a number of priority national projects of the Investment programs of the Republic of Uzbekistan.

Husan Hasanov (2020) Currently, IDB's portfolio in Uzbekistan is the largest in Central Asia (over \$1.8 billion).



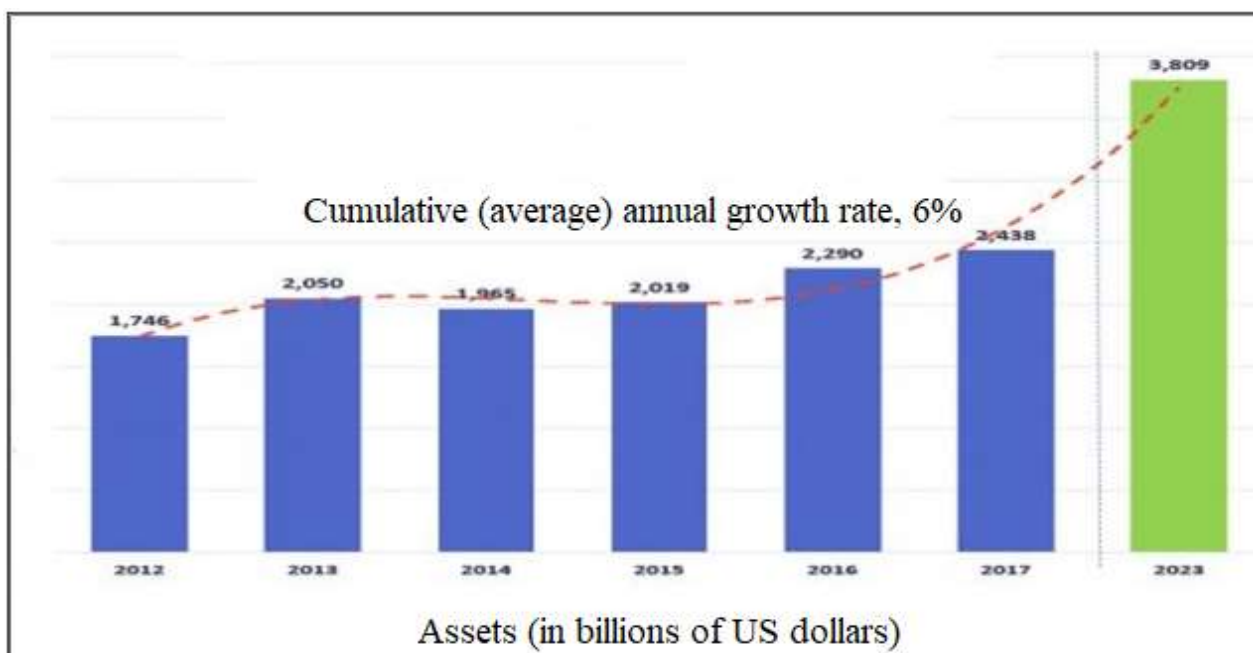


Figure 1. Growth of global financial institutions' assets rate institutions

By the beginning of 2019, the assets of Islamic finance reached almost 2.6 trillion US dollars. The account is expected to reach USD 3.4 trillion by the end of 2024 according to the books¹.

H. Smaoui & S. Nechi (2017) that Islamic finance managed to get a place on the agenda of the G20 increases its importance even more².

Since citizens and businessmen of our country are very interested in interest-free banking and financial services, a number of works are being carried out to form a system of providing Islamic financial services. Including:

- In the decree of the President of the Republic of Uzbekistan dated February 7, 2017 No. PF-N^o4947 "On the strategy of actions for the further development of the Republic of Uzbekistan", it is emphasized to take measures to expand cooperation with the Islamic Development Bank;

- Paragraph 2 of the decision of the President of the Republic of Uzbekistan dated March 5, 2019 "On measures to further expand and deepen partnership with the Islamic Development Bank Group and Arab Coordination Group Funds" states the main long-term partnership of the Republic of Uzbekistan with the IDB Group and AMG as one of its directions and tasks, the joint development and implementation of public-private partnership mechanisms, including support

programs through the establishment of endowment funds, and their implementation in Uzbekistan;

- The Islamic Development Bank and its group organizations, in particular the Private Sector Development Islamic Corporation (PSDIC), the International Islamic Trade Finance Corporation (ITFC) and the Islamic Research and Training Institute (IRTI) have been contributing to the development of Islamic finance in our country;

Daniyor Yuldashev (2021) The main difference between Islamic financial institutions and traditional financial institutions is that Islamic finance includes profit and loss sharing and financing based on real assets.

In other words, Islamic financing is based on partnership. Such institutions can build a facility, purchase equipment, raw materials or rent them at the customer's request. Funding is based on sales practices.

SETTING A SCIENTIFIC PROBLEM.

Many scientific works have been done, books have been written and definitions have been given on Islamic finance and its activities. In particular, in recent years, the theoretical and practical issues of Islamic finance have become one of the topical topics that are widely studied by foreign economists.

O. Trofimova (2009) in her scientific works highlighted the main aspects of the activity of Islamic finance in European countries and the necessity of its

¹<https://kun.uz/52711631?ysclid=18spazw7pf927347482;>

² <https://ideas.repec.org/a/eee/riibaf/v41y2017icp136-147.html>



application from a socio-economic point of view³.

Legal aspects of securities and contracts in Islamic finance were studied and analyzed by K. Batirova (2019)⁴.

V. Antropov (2017), one of the scientists of the CIS countries, in his scientific views, analyzed the organization of Islamic finance, the transactions used in it and their types, and the cases of using the services of Islamic finance in Europe and the USA⁵.

According to Dr. Abbas Mirahor, former Executive Director of the International Monetary Fund, Director General of the International Center for the Development of Islamic Financial Institutions and Chairman of the Islamic Education Center, and Zamir Iqbal, Director of Treasury Investments of the World Bank (2011), the Islamic system is characterized as a system that prohibits lending on the basis of interest⁶. Another group of researchers, Abbas Mirakhor and Mohsin Khan (2005), believe that such an interpretation is incomplete and leads to wrong conclusions⁷. According to them, the main elements of regulating the activities of the Islamic banking system in Islamic countries come from its obedience to Islamic laws. That is, the Islamic bank has a control system based on Islamic Sharia.

According to the research of Russian scholars Bekin (2008) and Kochmola (2007), Islamic financial institutions are successfully operating in countries where Islamic rules have not been fully implemented⁸

³ <https://cyberleninka.ru/article/n/musulmane-i-islam-v-zapadnoy-evrope>

⁴ https://tsul.uzweblines.com/storage/media/%D0%B7%D0%B0%D0%BA%D0%BE%D0%BD%D0%BE%D0%B4%D0%B0%D1%82%D0%B5%D0%BB%D1%8C%D1%81%D1%82%D0%B2%D0%BE/ozu_2_2019.pdf

⁵ <https://cyberleninka.ru/article/n/islamskie-finansy-v-globalnoy-ekonomike-sovremennye-tendentsii-i-perspektivy-prichiny-poyavleniya-islamskih-finansov/viewer>

⁶ Iqbal Z., Mirakhor A. (2011) An introduction to Islamic finance: theory and practice. Singapore: John Wiley & Sons (Asia) Pte. Ltd., 406 p.

⁷ <https://www.amazon.com/Theoretical-Studies-Islamic-Banking-Finance/dp/1889999407>

⁸ Bekkin R.I. (2008) Islamic Economics. Short course. M.: ACT East-West, 288 p.
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Table 1
Differences between Islamic banks and commercial banks⁹

Islamic banking services	Traditional banking services
Funding sources	Credits
Murobaha, salam, musharakah, istisnah, rent arrears	Working capital, fixed assets, leasing, microcredits
Investments	Deposits
Walia, loan, muzarabah, wakala	Current accounts, time deposits
Other services	Other services
Other Financial Services (Definitions Established Based on Shariah Principles)	Other financial services
Retail banking	Retail banking
Financing products	Consumer loans, auto loan, mortgage loan, credit cards, overdraft, overnight
Murobaha, salam, musharakah, istisnah, rent arrears	Deposits
Investment accounts	Current accounts, time deposits
Wadia, loan, muzarabah, wakala	Other services
Other services	Other financial services
Other Financial Services (Definitions Established Based on Shariah Principles)	

The literature on Islamic finance was translated from a foreign language into Uzbek by B. Joraev, an economist from Uzbekistan. (2014)¹⁰

The theoretical foundations of Islamic finance and financing through Islamic financial instruments are not fully explained in these scientific works.

In general, today Islamic finance is somewhat new for the world community and almost new for our national economy, so it is necessary to carry out many researches in the future.

⁹ Heydarov O'.A. Improving the use of the Islamic financial system in commercial banks of our republic. Scientific and practical journal of economics and finance No. 2 (150) 2022y 36 p.

¹⁰ Islamic finance and banking system. Translator: Botyrhoja Joraev. - T.: Uzbekistan, 2014. - 464 p.



RESEARCH METHODOLOGY. Scientific abstraction, grouping, comparison, retrospective and prospective, empirical analysis and 6 other methods were used in the research. In the article, the relevant conclusions were formed by comparing the organizational and legal basis of the methods of using Islamic financial instruments in world practice and developed commercial banks with the existing basis in our country.

ANALYSIS AND RESULTS.

We know that Islamic finance covers processes based on the principles and rules of Shariah in lending or financing, and makes transactions that are in accordance with the principles of Islamic finance. In this way, Islamic finance differs from conventional financing or lending. In particular, the attraction of funds in Islamic banking is carried out on the basis of partnership loan or deposit (deposit) contracts based on Sharia principles. In traditional banking, funds are attracted in return for guaranteed interest.

Table 2

Application of Islamic windows in commercial banks

№	Advantages of Islamic windows in commercial banks
1	Due to the attraction of financial resources from internal and external sources, additional financial resources appear in banks (that is, liquidity increases)
2	Banks achieve diversification of their assets and liabilities
3	Banks offer Islamic financial services in addition to their traditional services, thereby meeting the needs of their customers more fully.
4	The income from Islamic finance activities will increase the total income of the banks
5	The number of customers who currently do not use traditional banking services and products will be reached to use the products and services of Islamic branches, which will lead to a significant increase in the total number of customers of the bank.

The use of funds raised in Islamic banking is essentially different from traditional banking. Funds can be made according to the principles of Islamic finance, on the basis of sale, rent, leasing or partnership, or on the basis of financing and investment contracts.

In Islamic banking, we can see that Islamic window services and products compared to conventional banking services and products are listed in Table 1 above:

According to the official information above,

we can see that the financial services and products provided by Islamic banks are an alternative to the currently available conventional banking services and products, and at the same time, they are even flexible compared to conventional banking. For example, if we take the financing of fixed assets intended for legal entities, this type of financing can be carried out through Islamic banks in several ways (depending on the type of contract), depending on the client's financial situation, business plan and type of activity. "Islamic banking services window" - it is a separate structural unit that offers banking services based on Islamic principles within a traditional commercial bank, as opposed to an Islamic bank that does not provide traditional banking services at all.

Today, the "Islamic Corporation for the Development of Private Sector", a part of the "Islamic Development Bank" group, is actively working on the opening and development of branches that provide Islamic financial products and services ("Islamic branches") in several commercial banks of Uzbekistan.

Islamic branches are often established in countries where there is no Islamic financial system or legal framework for Islamic finance. Because, Islamic branches offer a limited number of services and products based on the existing laws and legal framework of a particular country as a product of a traditional banking division. Full-fledged Islamic banking services and products are usually provided after the relevant laws are developed in that country.

Commercial banks will have the following advantages when establishing the activity of Islamic branches in our country (*Table 2*).

Currently, there are about 1,400 Islamic financial institutions in more than 80 countries worldwide, according to the International Monetary Fund, which has shown the importance of Islamic financial institutions in the banking system over the past 10 years. It is noteworthy that Islamic financial institutions exist not only in Muslim countries, but also in European countries, countries where the Muslim community is a minority, such as Canada, the Philippines, and Singapore.

Also, today, the share of Islamic financial services is increasing in the world financial market, becoming one of the important sources of finance as a sector that includes innovative financing mechanisms. The fact that the total assets of Islamic financial institutions have reached 2.5 trillion dollars in recent years and are growing by 15-20% per year is a clear proof of



this¹¹.

With the aim of legal development of Islamic finance in our country, on September 4, 2021, the Islamic Development Bank allocated a technical assistance grant in the amount of USD 265,000 to support the development of the legal framework of Islamic banking and the financial sector. On December 20, 2017 "On measures to further increase the efficiency of cooperation with international and foreign financial institutions" and "Measures to further expand and deepen cooperation with Islamic Development Bank Group and Arab Coordination Group Funds" dated March 5, 2019 the decisions on these reforms serve as a legal basis.

"Islamic banking services window" is available at Amerisa Express Bank HSBC, ANZ Grindlays, BNP-Paribas, Chase Manhattan, UBS and many other first-tier banks. They have been providing all types of banking services that are fully compatible with traditional banking products in compliance with Sharia rules.

"Ipak Yuli" bank has always shown a great interest in actively participating in the project on the wide introduction of Islamic financing mechanisms in Uzbekistan, in particular, it is the first Uzbek bank that started cooperation with the Private Sector Development Islamic Corporation to provide financing to small and private business entities based on the principles of Islamic banking. Since 2006, "Ipak Yuli" Bank has provided a total of 22 mln. Funds in the amount of US dollars have been attracted. Within them, 43 projects were financed and more than 650 new jobs were created. "Silk Road" Bank has extensive experience and knowledge in the field of Islamic financing. This is the basis for the bank's successful implementation of the "Islamic Banking Services Window" project in Uzbekistan.

Work has begun on establishing an Islamic window in 14 banks in Uzbekistan. In particular, on February 8, 2021, Turon-bank, which is undergoing modern transformation processes, signed another important contract with Islam Corporation, which is a permanent and reliable partner in this direction, on the development of the private sector. According to him, now Turan Bank has begun consulting on the introduction of the Islamic banking system based on the principle of "Islamic Window" and implementing this system.

In fact, preparations for the launch of the "Islam window" at the "Turonbank" joint-stock commercial bank will undoubtedly give impetus to

the further expansion of mutual cooperation and the implementation of joint projects. As a result of this, the scope of services provided by the bank to the population will expand, it will be possible to rapidly develop entrepreneurship and small business, to create an instrument offering retail and corporate products based on Islamic principles. It should be said instead of information that Turonbank and the Islamic Corporation for the development of the private sector will invest 10 million in Jeddah in 2019. He signed the agreement on "Financing projects of small and medium-sized business entities" in US dollars. Within its framework, the production capacity of many enterprises was increased and new jobs were created.

Within the framework of the program of the 46th annual meeting of the Board of Directors of the Islamic Development Bank, JSC "Trustbank" signed an agreement with the Islamic Corporation in the amount of 10 million US dollars for the development of the private sector. This fund is planned to be directed to the development of areas such as health care, including the pharmaceutical sector, and the food industry. In addition, through this Islamic window, it is planned to offer financial services based on the principles of Islamic finance to the clients of "Trustbank" Private Joint Stock Bank.

On May 15-16, 2022, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) signed a cooperation agreement with the "Islamic Business and Finance" enterprise of Uzbekistan in Manama, the capital of Bahrain. Now, within the framework of this agreement, it will be possible to train, test and certify specialists in Uzbekistan based on the international standards (norms) of the accounting and auditing organization for Islamic financial institutions.

The center to be established in Uzbekistan is engaged in the training of specialists and organization of tests in the following areas:

- **Certified Professional Accountant in Islamic Finance (CIPA);**
- **Certified Shariah Consultant and Auditor (CSAA);**
- **Certificate of Proficiency in Financial Accounting Standards (CPFAS).**

Islamic branches, which have started operating in commercial banks of our country, are important in terms of the development of the banking system, the increase in the quality of financial services, the growth of the capacity of representatives of the private sector, the improvement of the standard of living of the population, and the contribution to the development of the country's economy.

¹¹https://islommoliyasi.uz/uz_islom-moliyasi-istiqboli/



CONCLUSIONS AND SUGGESTIONS.

As mentioned above, we can observe that the banks of Islamic countries have certain aspects. That is, in order to give loans based on Islamic principles, commercial banks will have to attract resources based on Islamic principles. In particular, if commercial banks provide loans to customers based on Islamic principles by attracting interest deposits, the bank's customers may not use this loan. Because deposit attraction does not meet the principle of Islam. In this regard, in our country, first of all, we need to do certain things to increase financial literacy in our society regarding Islamic finance.

In particular, taking into account that the current process of globalization is of urgent importance for the economy of our country, the creation of banking and financial services and products structure implemented on the basis of the principles of Islamic banking and finance, the following proposals were formulated:

1. It has provided new opportunities for conventional banks in areas where demand for Islamic banking is high. However, banks that want to open "Islamic windows" should have an independent Shariah committee with experts in Islamic jurisprudence, Islamic finance and law, as well as banking experts.

2. In order to use the instruments of Islamic finance, it is necessary to make changes to the current banking legislation, tax and civil codes and other legal documents or to adopt a separate law. It is also important to train personnel in this field and increase the literacy rate of the population.

3. One of the most important and outstanding features of Islamic finance is its asset-backed nature. In the traditional form of financing, banks and financial institutions work only with monetary units. That is why they prohibit trade in goods/products. In Islamic finance, money is not recognized as a commodity because it has no intrinsic value, it is only a medium of exchange. Islamic banks make a profit by selling something with intrinsic value for money at a premium. That is why, unlike traditional financial institutions, Islamic financing is asset-based.

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