

The Role of Islamic Loans in Advancing Financial Inclusion and Socio-Economic Development

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Abstract

This study explores the role of loans in Islam in fostering financial inclusion and addressing various economic and social challenges, particularly in Muslim-majority countries. By adopting a comparative research methodology, the research evaluates how Islamic loans differ from conventional financial instruments in promoting inclusive economic growth, alleviating poverty, and supporting community development. It investigates the challenges of Islamic loans, including accessibility, regulatory constraints, and cultural perceptions, while also exploring the potential benefits and limitations. Additionally, the study highlights the significant role of Islamic financial literacy in enhancing financial inclusion, focusing on how well-informed communities can better utilize Islamic financial services. The paper underscores the importance of Islamic finance, including tools like microfinance, zakat, and risk-sharing contracts, in contributing to poverty reduction, wealth redistribution, and overall economic stability. Through this analysis, the study presents a comprehensive understanding of how Islamic finance can serve as a powerful tool for sustainable economic development and financial inclusion.

Keywords: Access, Sadaqah, Qard Al-Hasan, Voluntary Charity, Zakat.

1. Introduction

Financial inclusion has become increasingly central to global development discussions, particularly as a means to enhance people's livelihoods, reduce poverty, and promote inclusive and sustainable growth. The importance of financial inclusion has grown within the frameworks of both the Millennium Development Goals (MDGs) and their successor, the Sustainable Development Goals (SDGs), particularly as they relate to improving access to finance for underserved populations. As part of this effort, financial institutions and policymakers in many developing countries are actively working to improve financial access for individuals and small businesses.

One of the key challenges for financial inclusion is to bridge the gap for people who lack access to formal financial services. Many individuals, especially those in emerging and developing economies, face barriers such as low income, lack of banking infrastructure, or cultural and religious considerations that make traditional financial systems inaccessible or unappealing. For instance, Islamic principles prohibit *riba* (interest), creating a need for alternative financing structures that align with religious beliefs. This has led to the development of Islamic finance as a viable alternative, with mechanisms like profit-sharing and risk-sharing, which aim to avoid exploitation and align with broader societal welfare.



Islamic finance, which emerged formally in the 1970s, is rooted in the Islamic moral economy—a framework that prioritizes the welfare of society (*maslahah*) and individual well-being. In this model, economic well-being is seen as a means to facilitate overall human flourishing, including spiritual well-being (*falah*) in this life and the hereafter. Tools like zakat (charitable giving) and waqf (endowment) have traditionally supported social welfare, and in modern market economies, Islamic financial institutions attempt to fill similar roles.

One example of Islamic financial inclusion is the *ar-rahn* and Zakat system. *Ar-rahn* provides short-term, Sharia-compliant loans by accepting jewelry or other items as collateral, which helps the unbanked meet their financial needs without interest. This service, which operates outside the formal banking sector, enables individuals to access financial resources while preserving religious principles, encouraging savings and investment, and contributing to economic well-being.

Studies exploring financial inclusion through *ar-rahn* show that it has had a positive impact on individual financial stability, especially for those who are excluded from formal credit markets. While Islamic banks face challenges in extending financial inclusion due to operational limitations and high costs, institutions like *ar-rahn* help address gaps by providing accessible, informal financing. Research into *ar-rahn*'s effects highlights the importance of alternative financial mechanisms aligning with economic and cultural needs, offering insights that could help shape financial inclusion policies and strategies for empowering underserved communities.

The research aims to find out:

- 1) To Examine how Islamic loans align with and differ from other financial instruments in promoting financial inclusion.
- 2) To Assess the impact of Islamic loans on economic and social issues in Muslim-majority countries, focusing on their role in poverty alleviation and community development.
- 3) To Investigate potential challenges and limitations in using Islamic loans to promote financial inclusion and address economic and social issues, considering factors like accessibility, regulatory constraints, and cultural perceptions.

2. Literature Review

A literature review by Najwa Al Swees on the topic of financial inclusion in the light of the Islamic economy examined the current research and studies on this topic in order to provide a comprehensive overview of the state of knowledge on this subject (Thomas, 2006). The review began by defining financial inclusion and discussing its importance in the context of global economic development. It then explored the position of the Islamic economy on financial inclusion, highlighting its support for efforts to provide financial services to the poor and marginalized and its reliance on non-usurious financing methods. This included a discussion of partnership contracts, such as *musharaka* and profit-sharing, as well as wealth redistribution instruments such as zakat and charity. The review also examined the role of the state in promoting financial inclusion through social financial inclusion tools, such as in-kind and cash assistance. In addition to discussing the various mechanisms through which the Islamic economy supports financial inclusion, the review by Najwa Al Swees also examined the challenges that needed to be addressed to effectively promote financial inclusion in the Islamic economic system. This included regulatory challenges, economic challenges, and other issues that may impact the ability of the Islamic economy to promote financial inclusion. Overall, the review by Najwa Al Swees provided a critical analysis of the current state of research on financial inclusion in the light of the Islamic economy, highlighting the strengths

and limitations of existing studies and identifying areas for future research. By synthesizing the available research on this topic, the review provided a valuable resource for scholars and policymakers interested in understanding the role of the Islamic economy in promoting financial inclusion .

In his study, Shaker Al-Samarrai (2018) investigates the role of Islamic banks in achieving the dimensions of financial inclusion in Jordan. Specifically, Al-Samarrai aims to identify the impact of various variables, such as gender, age, educational qualification, job nature, the bank that an individual deals with, and geographical location, on the role of Islamic banks in promoting financial inclusion. Al-Samarrai's research finds that Islamic banks in Jordan have higher customer access to banking services compared to conventional banks, particularly in terms of savings accounts and financing options for small and medium enterprises. Additionally, Islamic banks have a higher level of customer usage of banking services, with a focus on personal financing and investment products. The study also indicates that Islamic banks positively impact the dimensions of financial inclusion, including access, use, and quality of financial services. In particular, Islamic banks have been found to have a strong focus on providing access to financial services for underserved segments of the population, such as small businesses and rural communities. They also have a high level of customer satisfaction with the quality of their financial services. Based on these findings, Al-Samarrai recommends that Islamic banks work to enable individuals with crafts and professions and residents of remote areas to access financial services, and to innovate financing formulas that meet the needs of society, particularly youth. Overall, Al-Samarrai's study highlights the important role that Islamic banks play in promoting financial inclusion in Jordan.

3. Methods

A comparative method will be employed to investigate the role of loans in Islam in promoting financial inclusion and addressing economic and social issues. This method involves analyzing the effectiveness of Islamic loans relative to other financial instruments in fostering financial inclusion and addressing key economic and social challenges. The study will incorporate a variety of techniques to ensure comprehensive analysis and validation of findings.

1. Type of Article

This study will be a research article focused on empirical and theoretical analysis. The article will blend both qualitative and quantitative research methods to compare Islamic and conventional financial systems, specifically focusing on the role of loans in promoting financial inclusion. The primary aim is to produce findings that apply to policymakers, financial institutions, and researchers interested in the intersection of finance, social inclusion, and religious ethics.

2. Source of Data

The study will rely on secondary data sources to provide a well-rounded perspective:

Secondary Data:

Existing reports, academic papers, and government publications related to Islamic finance and financial inclusion. This includes financial inclusion indexes, poverty reduction reports, and publications by financial institutions like the World Bank, IMF, and regional financial bodies.

Historical data on the adoption of Islamic finance across various regions and its impact on economic development.

3. Data Collection Technique

Data collection will involve a combination of qualitative and quantitative methods to ensure the depth and reliability of the findings.

4. Results and Discussion

4.1. Barriers to Islamic Financial Literacy

Islamic financial literacy is becoming increasingly important in Muslim-majority countries, where Islamic finance significantly influences economic systems and daily financial transactions. Understanding the principles and mechanisms of Islamic finance allows individuals and businesses to make informed financial decisions that align with their cultural and religious beliefs. This knowledge—encompassing awareness of Islamic banking, financial products, and services—can greatly influence financial inclusion, particularly among underrepresented groups (Hassan, 2024).

Studies highlight the positive relationship between Islamic financial literacy and financial inclusion. For example, in Indonesia, micro-enterprises with a solid grasp of Islamic finance concepts tend to show improved business performance and are more likely to access financial services. This access often translates into increased economic resilience and growth for these businesses. In Turkey, research has shown that university students with prior exposure to Islamic finance demonstrate higher levels of understanding, suggesting that early education can play a crucial role in building financial literacy. However, there are gaps in data for countries like Nigeria, where the influence of Islamic financial literacy on economic growth and financial inclusion remains under-researched, underscoring the need for targeted studies to capture its impact in diverse contexts (Novreska & Arundina, 2024).

The potential of Islamic financial literacy to support economic growth is evident in the link between financial inclusion and economic development. In developing economies, increased access to financial services often means more opportunities for individuals to invest in health, education, and business, ultimately contributing to poverty reduction and enhanced human development. The integration of Islamic finance into mainstream financial systems could be particularly beneficial for underserved populations in Muslim-majority countries, where inclusive access can promote long-term economic growth.

Yet, there are challenges to boosting Islamic financial literacy. Many people still lack basic financial literacy, are unaware of Islamic financial options, or face cultural barriers that hinder their participation in formal financial systems. Additionally, there are few standardized educational tools or resources available to measure and promote Islamic financial literacy comprehensively (Er & Mutlu, 2017)

To address these challenges, several policy measures could prove effective. Tailored educational programs for small business owners could improve their financial skills and broaden their access to financial services. Specialized training initiatives that teach practical financial management skills in an Islamic finance context can empower individuals, making it easier for them to access suitable financial products. Encouraging partnerships between micro-enterprises and Islamic banks may also facilitate better access to growth resources, while supportive policy frameworks could promote Islamic finance as a viable tool for economic development.

Islamic financial literacy holds the potential to drive economic growth and financial inclusion in Muslim-majority countries. By addressing current challenges and implementing targeted education and policy initiatives, these countries can not only expand access to financial services but also improve overall quality of life. Investing in awareness and education

around Islamic finance is essential for fully unlocking its developmental potential, allowing Islamic finance to act as a robust driver of economic progress (Mustafa et al., 2018).

4.2. The landscape of financial inclusion for Muslim regions

Financial inclusion is a critical aspect of economic development, particularly for marginalized populations. Among Muslims, various barriers hinder access to formal banking services, leading to significant disparities in financial inclusion compared to non-Muslims.

The landscape of financial inclusion for Muslims varies significantly across different regions. In high-income countries, Muslims generally have better access to banking services compared to their counterparts in lower-income regions, such as Sub-Saharan Africa and East Asia. Factors such as the presence of Islamic financial institutions, regulatory frameworks, and cultural attitudes towards banking play a crucial role in shaping these disparities. For instance, in countries with a dual-banking system, like Malaysia and Indonesia, Islamic banks coexist with conventional banks, leading to varying degrees of accessibility and acceptance among the population. Despite a high awareness of Islamic banking products (48% in some regions), actual usage remains low, with only 2% of adults reporting current use of Sharia-compliant services. This gap highlights the need for targeted strategies to enhance financial inclusion in regions where access is limited (Elfi et al., 2024).

Education is often considered a key determinant of financial behaviors and preferences. However, the analysis indicates that financial inclusion patterns among subpopulations, including education levels, do not differ significantly between Muslims and non-Muslims. This suggests that while education may influence financial behaviors, it is not the primary barrier to financial inclusion. Instead, factors such as cost, distance to banking services, and documentation requirements are more prominent. Further research is needed to explore the nuances of how education specifically affects financial behaviors among Muslims compared to non-Muslims, as understanding these dynamics could inform more effective financial inclusion strategies.

While the document does not explicitly address the role of technology access in financial inclusion, it is reasonable to infer that technology could play a significant role in overcoming barriers faced by both Muslims and non-Muslims. Access to technology can facilitate easier communication with financial institutions, provide information about available services, and streamline the documentation process. However, the existing barriers of cost, distance, and documentation remain critical challenges that need to be addressed to improve financial inclusion for Muslims. Further investigation into the impact of technology access on financial inclusion is warranted, as it may reveal additional insights into how to bridge the gap between awareness and actual usage of financial services (Mustafa et al., 2018).

The analysis of barriers to financial inclusion for Muslims reveals a complex interplay of regional variations, education, and technology access. While awareness of Islamic banking products is relatively high, actual usage remains low, indicating a significant gap that needs to be addressed. Policymakers and financial institutions should focus on enhancing education and outreach efforts to raise awareness about Sharia-compliant products and their benefits. Additionally, improving access to technology and addressing the fundamental barriers of cost, distance, and documentation will be essential in promoting financial inclusion among Muslim populations. By adopting a multifaceted approach, it is possible to create a more inclusive financial landscape that aligns with the values and needs of Muslim communities (Elfi et al., 2024)

Islamic banks face several regulatory challenges that vary across different jurisdictions, often impacting their operations and stability. Key issues include:

1. **Misaligned Regulatory Frameworks:** Many Islamic banks are subject to conventional banking regulations that don't fully accommodate their unique characteristics. This mismatch can lead to inefficiencies and regulatory risks.
2. **Profit-Sharing Investment Accounts (PSIA):** PSIA are often classified as deposits by regulators, which undermines their role in absorbing losses. This misclassification increases systemic risks and complicates capital management for Islamic banks.
3. **Displaced Commercial Risk:** Islamic banks may feel compelled to offer competitive returns to attract customers, which can strain their reserve-building efforts and complicate regulatory capital calculations, especially in competitive markets.
4. **Lack of Harmonization:** There is significant variation in *Shari'ah* governance practices and regulations across different regions. This lack of standardization can lead to regulatory arbitrage, making cross-border operations more difficult.
5. **Shortage of Qualified *Shari'ah* Scholars:** The limited number of *Shari'ah* scholars with expertise in Islamic finance can slow down the development of new Islamic financial products, hindering growth and competitiveness.
6. **Global Banking Standards vs. Islamic Finance Principles:** National authorities often prioritize global conventional banking standards over Islamic finance principles, which can lead to inadequate application of regulations specific to Islamic finance.
7. **Liquidity Management Issues:** Islamic banks face challenges in meeting Basel III liquidity requirements due to a lack of *Shari'ah*-compliant high-quality liquid assets (HQLA), complicating their ability to maintain adequate liquidity coverage ratios.

These challenges highlight the need for more tailored regulatory frameworks and greater international collaboration to support the growth and stability of Islamic banking (Kammer et al., 2015).

4.3. Importance of Islamic Finance for Financial Inclusion

Islamic finance offers a unique approach to financial inclusion, particularly in markets with significant Muslim populations, by providing access to services that align with ethical and religious values. According to the 2023 Islamic Financial Services Industry Stability Report from the Islamic Financial Services Board, the global Islamic financial services sector—which includes banking, capital markets, and takaful (Islamic insurance)—reached an estimated USD 3.25 trillion in 2022, showing a steady annual growth rate of 6.2%. This expansion highlights the increasing role of Islamic finance in creating inclusive economic systems through diverse, faith-compliant products (Lone & Karima, 2019)

Islamic finance's core segment promoting financial inclusion is Islamic microfinance, which addresses financing needs in low-income communities. Islamic microfinance provides ethical, accessible financial services that align with social principles, like caring for the less fortunate. By focusing on underserved populations, it offers a socially responsible alternative to conventional finance, thereby fostering economic empowerment and reducing poverty. Programs often specifically target women, enabling them to access small loans to launch or grow businesses, creating income-generating opportunities and supporting community welfare (Jouti, 2018).

The role of Islamic finance in supporting national financial inclusion strategies (NFIS) has also gained attention. Countries such as Malaysia, Nigeria, the Philippines, and Palestine explicitly include Islamic finance within their NFIS, recognizing its potential to reach populations typically excluded from traditional finance. Other nations, including Sudan and the Maldives, are incorporating Islamic finance into their developing NFIS frameworks, showing a growing acknowledgment of its ability to meet financial inclusion goals.

Islamic finance also introduces risk-sharing contracts, which serve as alternatives to debt-based financing. This structure promotes a more sustainable economic model, as it reduces borrowers' financial distress risk by sharing potential profits and losses. Additionally, Islamic finance supports wealth redistribution through instruments such as Zakat (almsgiving) and Waqf (endowments), reinforcing its alignment with social justice goals and Sustainable Development Goals (SDGs) like poverty reduction (Khuri, 2014).

While Islamic finance presents promising avenues for financial inclusion, challenges remain. Some countries with established conventional finance systems face integration hurdles, and limited understanding of Islamic finance principles among policymakers can hinder adoption. Knowledge-sharing, research, and awareness initiatives are essential to bridge these gaps and unlock the potential of Islamic finance for inclusive financial systems globally (Thomas, 2006).

4.4. Tools Of Financial Inclusion In The Islamic Economy

Loans in Islam are seen as a valuable solution for addressing economic and social issues in our society. For example, many young people have recently graduated from universities, institutes, and technical schools, but cannot find employment due to layoffs and company closures. These individuals may benefit from loans to start small projects that align with their skills and interests, including agricultural, industrial, and commercial ventures. Additionally, loans may be useful in addressing issues related to informal settlements, such as the lack of basic services like drinking water, sewage, and environmental pollution caused by waste accumulation. Overall, loans in Islam can help to create job opportunities and address social and economic problems in our nation. As we have explained, the loan in Islam is the most appropriate and important means to revitalize society, spread security and peace in its neighborhoods, and lead to economic prosperity and solve social problems. This is because we have derived from what has been mentioned earlier:

First: The loan preserves the dignity of the indebted person from begging and opens the door of hope for him to work and live from it. Second, returning the loan to the lender is also better than the lender not wanting to accept the gift and hide the loan, which is prohibited in Islam. Third, the loan also stimulates economic activity and contributes to the spread of social peace (Halim, 2014).

In conclusion, the loan in Islam is a great blessing with many benefits and virtues, and it is one of the most important means of social and economic development. It is also a moral and humanitarian duty imposed on every Muslim who can help others and respond to their needs.

The good loan has two benefits; the first is spiritual, which is the reward of Allah, the Exalted, for lending money with the blessings of their money in this world and forgiveness of their sins in the Hereafter. Allah says,

“If you lend Allah a good loan, He will multiply it for you and forgive you, and Allah is appreciative and forbearing.”

It has been previously mentioned that the loan is multiplied by eighteen.

The second benefit of a good loan in Islam is a material benefit, which is the exemption of the lender from paying zakat on their loans to others, according to scholars of the Hanafi and Maliki schools. Zakat is a charitable gift paid annually as a percentage of one's wealth and distributed to the poor within a specific geographic area. The percentage required for zakat varies based on the type of wealth and its value. For example, in trade, zakat is calculated at one fortieth of the total wealth, while for shepherds, zakat is calculated based on the number of sheep, cows, and camels they own. Therefore, the exemption from zakat on loans to others

is an important incentive for giving a good loan, in addition to the fact that loans are an effective way to combat hoarding (Farhat, 2023).

Money is considered a mandatory payment to the deserving poor annually, while sheep, camels, and cows represent the poor's self-sufficiency through animal husbandry and reproduction. Zakat is one of the main financial tools used by Islam in the economy to meet the needs of the Islamic community, achieve stability and worldly happiness, and if desired, eternal happiness as well, since Islam does not impose or force eternal happiness.

Islam encourages Zakat as it is an important matter that guides worshipers and countries. It leads to the widespread adoption of social solidarity and solidarity, which increases the cohesion of community members and reflects this cohesion on all systems that adopt it, whether political, economic, or other. This reflects its dignity in front of other countries and societies that respect their interests and interests, but not to the extent of imposing their will on them as much as it is reflected in building and protecting the interior in front of these countries and societies (Warsame, 2009).

In the absence of Zakat and neglect of the social sectors, its targets, social, political, and economic cohesion will be undermined. The absence of zakat, a charitable gift paid annually as a percentage of one's wealth and distributed to the poor within a specific geographic area, can lead to an increase in poverty and social unrest. It can also contribute to the widening of class differences and internal conflicts as people struggle to meet their needs. The psychological impact of zakat's absence can also fuel negative emotions such as envy, hatred, and even violence, leading to chaos and corruption. This can weaken a society's internal defences and reduce its power and dignity in the eyes of the outside world. It becomes weak and unable to meet its requirements. Therefore, it kneels to the countries and societies that respect its interests and plans (Abdullah, 2024).

Islam emphasizes the importance of zakat (alms-giving) as a tool for building strong communities and nations. By promoting the distribution of wealth among the poor and needy, zakat helps to foster social cohesion and solidarity. This strengthens a society's political and economic systems and helps protect it from internal conflicts and external threats. Furthermore, the Islamic concept of zakat encourages self-sufficiency and independence, as it emphasizes the importance of individual responsibility for one's own well-being and the well-being of others. This is in contrast to the idea of relying on others or being dependent on external sources of support. In terms of the distribution of any surplus zakat funds, Islam prohibits hoarding and greed. Therefore, any excess funds would be used for productive purposes, such as investment in economic activities that benefit the community. This approach helps promote economic growth and stability, increasing the power and influence of Islam and its followers. Ultimately, the goal of zakat is to create a just and equitable society where all individuals have access to the resources they need to live fulfilling lives. By promoting social harmony and economic development, zakat helps to bring about peace and security in the world. Islam encourages the practice of zakat, as it is considered an important aspect of Muslims' religious and social life. Zakat promotes the values of social solidarity and mutual support, strengthening the bonds within the community and reflecting positively on all aspects of society, including political, economic, and other systems.

This in turn enhances the dignity and power of the Islamic state and society, increasing Islam's popularity among people seeking peace and security. Zakat is a mandatory form of charity that is required of all Muslims who are financially able to do so. It is based on the principle of wealth redistribution, ensuring that the wealth of the community is distributed fairly and equitably among its members. This helps to reduce poverty and inequality, and promotes social cohesion and stability. However, the consequences can be severe if zakat is

not distributed properly or if social welfare programs are neglected. This can lead to a decline in social and political cohesion, increased poverty and inequality, and even violence and conflict. Therefore, it is important that zakat is collected and distributed fairly and transparently, in accordance with Islamic principles (Kashi, 2017).

If there is a surplus of zakat (Islamic tax) after it has been distributed to its rightful recipients, this surplus should be used for the benefit of the community. Islam prohibits hoarding and exploitation of others; therefore, the surplus should be used for productive purposes, such as investment in economic development and export activities. This will help strengthen the economy and increase the Islamic state's and society's self-sufficiency. Overall, zakat is an essential component of the Islamic economic system, as it helps to fulfill the basic needs of the disadvantaged members of society, promotes social justice and fairness, and strengthens the overall economy and society. If the zakat is applied as Islam intends, its impact will be limited to many individuals in the community. However, if it is applied correctly, it can lead the community from backwardness to progress, and guide the development path in every Islamic society. Zakat is not just a personal relationship between the wealthy and the poor but a relationship between the state and its citizens. Therefore, the state should take zakat from the wealthy and spend it on projects that will lift the poor to the level of the wealthy. (Faudel., 2012) Zakat is not a temporary charity, but rather a complete wealth. Our prophet, Omar, said to those responsible for collecting zakat:

“If you give, then you will become wealthy,”

And Naway said:

“The poor and the needy are given what will lift them from poverty to wealth without becoming poor again,”

Even this small part of the Islamic economy, which some see as isolated, can lead to economic progress if understood as intended by God as a tool for production and a means of progress. The economic problem lies in the existence of misguided wealth and unaddressed poverty. Both provision and the provider are blessed, and the power is measured on earth, as God says:

“And in it are its forces measured.’ But work and effort to seek provision are not equal among people. Some work hard and get little, while others do little and get a lot. This imbalance leads to injustice and inequality. Islam came to correct this imbalance and establish justice by obligating the wealthy to pay zakat and spend it on the poor and needy. This creates a balance in society and helps the poor rise to the level of the wealthy. This is the role of zakat in the Islamic economy” (Muhammad et al., 2021).

4.5. Accessing Financial Services through Islamic Finance

Islamic finance is vital in promoting financial inclusion, particularly in Muslim-majority countries, where it aligns financial services with religious values and ethical principles. Here's a closer look at how Islamic finance supports financial inclusion and the broader economic benefits it brings:

1. **Access to Financial Services:** One of the main benefits of Islamic finance is its ability to provide financial products that comply with Sharia (Islamic law), which prohibits interest-based transactions and speculative investments. This feature is crucial for individuals who avoid conventional banking due to religious beliefs. By offering alternative products like Islamic microfinance and risk-sharing contracts (such as *Musharakah*, or partnership-based agreements), Islamic finance makes financial services accessible to low-income populations. These services allow individuals to participate in the financial system, giving them opportunities to save, invest, and grow financially without compromising their religious principles. The financial behaviors of Muslims compared to non-Muslims show

significant differences in terms of account ownership and savings. Muslims are significantly less likely than non-Muslims to own a formal account or save at a formal financial institution, even when controlling for other individual and country-level characteristics. Specifically, self-identification as a Muslim is associated with a 6 percent decrease in the probability of having a formal account compared to non-Muslims. However, there is no evidence that Muslims are less likely than non-Muslims to report formal or informal borrowing.

2. **Poverty Alleviation:** Islamic finance has a strong focus on poverty reduction through tailored products like micro-takaful (Islamic microinsurance) and Islamic microfinance. These products are designed to support the poor and underprivileged, offering them the chance to access funds for crucial investments in education, health, and business. For example, with Islamic microfinance, people in low-income communities can secure small, interest-free loans or participate in profit-sharing contracts to launch small businesses. Such access to capital helps lift individuals and families out of poverty by providing them with a means to generate income and build sustainable livelihoods.
3. **Wealth Redistribution:** Unlike conventional finance, Islamic finance includes built-in mechanisms for wealth redistribution, which are intended to support social welfare and economic stability. These mechanisms include zakat (mandatory charitable giving), *sadaqah* (voluntary charity), and *qard al-hassan* (interest-free loans for those in need). Through zakat, for instance, a portion of wealth from the financially well-off is redistributed to support those in need. This redistribution helps to reduce wealth inequality and ensures a more balanced flow of resources, especially in communities where access to capital is limited.
4. **Economic Development:** Islamic finance contributes to economic growth by promoting financial inclusion, which allows more people and small businesses to participate in economic activities. When individuals and small enterprises gain access to capital, they can invest in expanding their operations, creating jobs, and boosting local economies. The emphasis on ethical financing and risk-sharing also promotes more responsible investments and reduces the likelihood of financial crises, as seen during the 2008 financial crisis, when Islamic financial institutions were relatively insulated due to their avoidance of high-risk and speculative activities.
5. **Reduction of Income Inequality:** One of the core objectives of Islamic finance is to reduce income inequality by providing financial opportunities for underserved communities. Islamic finance aims to bridge the gap between the wealthy and the less privileged by promoting an equitable distribution of resources. By focusing on socially responsible investments and supporting financial inclusion, it enables marginalized populations to improve their economic standing, contributing to a fairer society overall. Higher income levels are positively associated with both awareness and use of Sharia-compliant banking products.
6. **Access to Media:** Having a television and internet access is strongly related to both awareness and use of Islamic banking services.
7. **Gender:** Females are significantly less likely to report using Sharia-compliant banking services compared to males.

The Islamic finance is an essential tool for promoting financial inclusion in Muslim-majority countries, offering services that respect religious beliefs while fostering economic growth and social stability. By providing access to capital, reducing poverty, redistributing wealth, and supporting underserved communities, Islamic finance contributes not only to the

well-being of individuals but also to the overall development of inclusive and sustainable economies (Novreska & Arundina, 2024).

The facts and reality will be shown as:

1. **Islamic Banking Assets Growth:** The growth trend of Islamic banking assets from 2008 to 2014 shows significant increases across various regions, including the Gulf Cooperation Council (GCC), Middle East and North Africa (MENA) (excluding GCC), Sub-Saharan Africa, and Asia. This trend highlights the expanding footprint of Islamic finance globally.
2. **Compound Annual Growth Rate (CAGR):** Between 2009 and 2013, countries such as Bahrain, Kuwait, UAE, Saudi Arabia, Malaysia, Turkey, Pakistan, Qatar, and Indonesia exhibited varying CAGRs in Islamic banking assets, indicating robust growth in these markets. This data underscores the increasing acceptance and integration of Islamic banking within the global financial system.
3. **Volume by Issuer:** The distribution of volume by issuer reveals that governments account for 48% of the issuance, followed by financials at 23%, and other sectors such as industrials (9%), utilities (9%), consumer discretionary (4%), materials (2%), and others (4%). This breakdown illustrates the diverse sources of Sukuk issuance and the role of Islamic finance in the public and private sectors.
4. **Regulatory Frameworks:** The need for a unified regulatory framework for Islamic banks is emphasised, as current regulations often differ significantly from those governing conventional banks. This inconsistency can create challenges for Islamic banks in terms of compliance and operational efficiency.
5. **Challenges with Basel III:** Islamic banks face specific challenges in implementing the Basel III Accord, particularly regarding the classification of instruments eligible for Tier 1 and Tier 2 capital. The scarcity of *Shari'ah*-compliant high-quality liquid assets (HQLA) complicates their ability to meet liquidity coverage ratio (LCR) requirements, highlighting the need for tailored regulatory solutions (Kammer et al., 2015).

5. Conclusion

In conclusion, the integration of Islamic finance into broader financial systems offers a promising path toward enhancing financial inclusion, especially for underserved populations. By combining the ethical principles of Islamic finance with innovative financial mechanisms, policymakers, financial institutions, and researchers can foster a more inclusive and sustainable financial ecosystem. The key to success lies in addressing regulatory, infrastructural, and cultural challenges, as well as promoting financial literacy and awareness within communities.

Financial institutions should focus on developing products that cater to the diverse needs of individuals, businesses, and communities, leveraging technology to make these products more accessible. Additionally, fostering partnerships with international bodies and local communities can help build trust and create a more conducive environment for the growth of Islamic finance. Policymakers must also ensure that the legal and regulatory frameworks support the expansion of Islamic finance while addressing the specific needs of small and medium-sized enterprises (SMEs) and vulnerable populations.

Research into the impact of Islamic financial instruments, such as Islamic loans, on poverty alleviation and social welfare is essential to refine and optimize these mechanisms. With continuous evaluation and a focus on measurable outcomes, Islamic finance can effectively contribute to the achievement of Sustainable Development Goals (SDGs), promoting poverty reduction, economic growth, and social equity.

By recognizing Islamic finance's potential and creating a conducive environment for its growth, stakeholders can significantly enhance financial inclusion, reduce economic inequality, and empower underserved communities. Combining ethical principles with innovative financial solutions offers a holistic approach to addressing economic and social challenges, driving forward the vision of an inclusive global financial system.

For policymakers, it is crucial to create supportive regulatory frameworks that allow Islamic finance to thrive while ensuring that these systems are transparent, accessible, and adaptable to different contexts. Financial institutions are encouraged to innovate and expand product offerings, ensuring that financial services are more inclusive, particularly for the unbanked and marginalized populations. Researchers should continue to explore the impact of Islamic finance in different socio-economic settings, focusing on its potential to address global challenges like poverty, inequality, and economic instability. Together, these efforts can help create a financial system that is both ethical and inclusive, benefiting individuals, businesses, and communities across the globe.

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