

A COMPREHENSIVE EXAMINATION OF ISLAMIC FINANCE OPPORTUNITIES IN UZBEKISTAN'S TRANSPORTATION INDUSTRY

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Abstract

Islamic banking, which adheres to Sharia principles, is a growing field of interest in Uzbekistan. In Central Asia, only Turkmenistan and Uzbekistan are yet to establish comprehensive Islamic banking services (Tursunov A., 2021). While the country lacks full-fledged Islamic banks, positive developments are suggesting a potential future for Islamic finance instruments. The current article examines the current landscape and emerging trends in Islamic finance and its future in Uzbekistan article provides an overview of Islamic banking and finance in Uzbekistan, along with suggestions for employing specific types of Islamic finance tailored to the needs of different customer segments.

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Introduction

Uzbekistan, with a Muslim population exceeding 90%, presents a significant potential for Islamic financial institutions to play a crucial role in the country's economic development. Islamic banking and finance (IBF) rapidly growing sector with significant potential in Uzbekistan (Entrepreneurship, 2024).

Even Uzbekistan's IBF landscape is still in its early stages, some [conventional banks offer "Islamic windows" with Sharia-compliant products (UNDP, 2020). The Islamic Development Bank (ICD) has partnered with Uzbek banks for financing projects based on Islamic principles, particularly Murabaha (cost-plus financing) (UzDaily, 2012). This collaboration highlights Uzbekistan's growing interest in IBF.

Potential Market

A UNDP study revealed that over half (56%) of individuals and 38% of businesses avoid conventional loans due to religious beliefs (Entrepreneurship, 2024). However, public awareness about IBF instruments remains low (UNDP, 2020). It could be seen as evidence of a significant potential market. Drawing funds from existing banks towards Islamic-aligned financing aids in bolstering the socio-economic development of Uzbekistan and its private sector (Tursunov A. S., 2020).

Regulatory status

In Uzbekistan, the legislation on Islamic finance is constantly being improved. In particular, within the framework of the decree of the President of the Republic of Uzbekistan dated September 11, 2023, on the "Uzbekistan - 2030" strategy, it is determined to accelerate reforms in the banking system, increase the size of the banking services market and develop competition in the sector. This task includes the

introduction of Islamic finance criteria and procedures in at least 3 commercial banks and the formation of the legal basis of Islamic finance. (Lex.uz, 2023)

Current legislation has yet to be improved to fully function. There is an opportunity and a legal basis for Islamic finance in a broad sense in the legislation of Uzbekistan. That is, there is a principle of freedom of contracts. However, there are obstacles in the law for Islamic banks. That is, the law on banks prohibits banks from trading. The activity of Islamic banks is based on commerce. In the new draft law, Islamic banks are allowed to engage in trading activities. There is a question of additional taxation in this place, therefore certain tax benefits are given (Kun.uz, 2023).

Potential Benefits

The introduction of a robust Islamic financial system in Uzbekistan can offer several advantages:

- **Financial Inclusion:** Islamic financial instruments based on profit-sharing and asset-based financing can address the financing needs currently unmet by conventional banking, particularly for Micro, Small, and Medium Enterprises in the transport sector.
- **Reduced Financing Costs:** Islamic financing can potentially offer more competitive financing rates compared to conventional banking, promoting investment and economic activity in the transport sector.
- **Ethical Considerations:** For individuals and businesses seeking Sharia-compliant financial instruments, IFIs can provide ethical alternatives to conventional banking practices that involve interest (riba), which is prohibited in Islam.

Recommendations

Given the predominantly Muslim population and the segmentation within it, coupled with the current developmental stage, specific Islamic finance instruments could notably enhance financial inclusion, particularly in the transportation sector. Instruments such as Mudarabah, Musharakah, and Ijarah could be effectively utilized:

- **Mudarabah.** This profit-sharing arrangement involves one party providing the capital (Rabb-ul-Maal) while the other party manages the business (Mudarib) (Gardezi, 2023). In the context of the transportation sector, Mudarabah could facilitate the acquisition of vehicles or infrastructure development, where investors provide funds while transportation operators manage the business, sharing profits accordingly. This arrangement fosters risk-sharing and encourages entrepreneurial activities.
- **Musharakah.** This is a form of partnership where partners contribute capital and share profits and losses (Adzimatunur, 2020). In the transportation sector, Musharakah could be utilized for large-scale projects such as building transportation hubs or purchasing fleets of vehicles. Investors and operators would collaborate, sharing both financial risks and rewards. This model promotes equity and collective responsibility, aligning with Islamic principles.
- **Ijarah.** This refers to leasing or rental contracts where the lessor retains ownership while the lessee pays rent for the use of the asset. In transportation, Ijarah could facilitate access to vehicles for individuals or businesses unable to afford outright purchase. This arrangement allows for flexibility in fleet management and ensures access to essential transportation services without the burden of ownership. It promotes accessibility and affordability while adhering to Islamic finance principles.

Conclusion

By employing these Islamic finance instruments tailored to the transportation sector's needs and the Muslim-majority population's preferences, financial inclusion can be significantly enhanced. This

approach fosters economic growth, promotes equitable access to transportation services, and aligns with the values and principles of Islamic finance.

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