ISLAMIC FINANCIAL SERVICES AND BANKING IN UZBEKISTAN AND CENTRAL ASIA

MURTOZAKHUJAEV SULTONKHON MUNAVVARKHUJA UGLI
Business Administration, STARS International University in Tashkent
sultonkhonmurtozakhujaev@gmail.com
Yoqubova Nigora Nizomiddinovna
STARS International University in Tashkent Senior Teacher
eshmurodovanigora707@gmail.com
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Abstract: *This article examines the problems related to Islamic banking and finance, working on the basis of Islamic law, and presents opportunities and obstacles of Islamic banking in Central Asia and Uzbekistan.*

Key words: *Islamic Financial, Islamic law, SDG, World Bank, Musharakah, Mudarabah, Sukuk issues, AAOIFI, IFSB, IIFM, Emerging Market, Islamic Retail Banking, Islamic Micro-Financing, Eco Islamic Bank, National Bank, GDB, OIC member countries, Al-Hilal Bank.*

WHAT IS THE ISLAMIC FINANCE AND BANKING?

Islamic Financial system is an integral system in which all financial activities are carried out based on Islamic law (Sharia) with risks and profits shared amongst all parties, while justice and fairness are ensured in any related transaction. It facilitates the flow of money within the economy, boosts economic activity, and prevents the concentration of capital in fewer hands. Uzbekistan is a country in Central Asia with an emerging economy with great human capital, an openness to micro-investments, and a high encouragement of small and medium businesses. Small and medium enterprises represent 70 percent of the economic landscape and 78 percent of the employment rate in the country. However, small and medium-sized enterprises are facing many challenges such as the high-interest rates and complicated loan requirements. Similarly, many Muslim citizens in Uzbekistan with capital in hand, are facing difficulties in dealing with banks in terms of investment activities due to the interest rates involved. The latter implies that individuals and enterprises do not get sufficient financing for boosting and maintaining their cash flows and revenue growth. Therefore, there is an essential need to understand the prospects of implementing a solid and integral Islamic Financial System in a country with a Muslim majority population.

This report attempts to explore the opportunities and to propose the necessary steps and procedures for implementing a solid Islamic banking and finance system in the Republic of Uzbekistan.

The report's first section begins with a summary of the country's current financial system, including information on how small, medium-sized, and large businesses can get credit, how they contribute to the nation's economy, and what major obstacles they face. The second section lists many Islamic finance instruments and the conditions necessary for their use, with a focus on those that Islamic finance institutions around the globe use without exception. Also covered by the author are the tools that may be used operationally in Uzbekistan and the legal situation of the country's future Islamic finance sector. The final section of the research examines the potential applications of Islamic finance to the SDGs and the integration of Islamic social finance elements into Uzbekistan's financial system (waqf, zakat, crowdfunding). The last section includes a descriptive analysis based on surveys that examine Uzbek populations' (individuals, businesses, and banks) preferences and demand for Islamic finance instruments, as well as the difficulties they face in obtaining the funding they require from the nation's current financial institutions. The recommendations drawn from the study are included at the end of the report. The debate over Islamic finance's origins and method of operation is active and always evolving. To fully develop the concept of a financial system based entirely on the real economy, some scholars contend that a world order based on the Qur'an is necessary (Choudhury, 2007). Instead, proponents like Yerlan Baitaulet, the chairman of the Association of Islamic Bankers in Kazakhstan, see the development of Islamic finance as a new branch of contemporary finance ethical banking

PRINCIPLES OF ISLAMIC FINANCE

Islamic finance is an equity-based, asset-backed, ethical, sustainable, environmentally, and socially responsible finance. It promotes risk sharing, connects the financial sector with the real economy, and emphasizes financial inclusion and social welfare (World Bank, 2015). Iqbal (1997) defined Islamic finance as a system that aims to make an actual and moral distribution of resources and promotes social fairness in a society. The main principles of Islamic Finance include the prohibition of interest and late payment fees; avoidance of excess uncertainty in financial transactions; financing linked to real assets; partnership and returns linked to risk; prohibition of investing in unethical businesses (e.g., alcohol production, etc.). Islamic finance contracts fall under one of the following categories: Profit-and loss sharing (PLS), sale-based contracts, and fee-based instruments. PLS financing is considered the closest to the spirit of Islamic finance compared to sale-based and fee-based instruments. The key principles of PLS based financing are equity and participation, and it is linked to real economic activities to assist the equitable distribution of income. There are two types of PLC financing models: Musharakah and Mudarabah. Sale-Based products are widely used in practice by Islamic financial institutions. These products are used to finance consumer and corporate credit, rental, and manufacturing. These products are Murabahah, Ijara, Salam, and Istisna. Fee-Based Products include Wakalah, Kafalah, or Ju'alah and are offered by Islamic banks as an auxiliary to Murabaha and Mudaraba transactions. Fee-based products are also used for bank transfers, letters of credit and guarantees, credit cards, etc. These instruments serve as the basic building blocks for developing a wide array of more complex financial instruments, suggesting that there is a great potential for financial innovation and expansion in Islamic financial markets

The discussion about the foundation of Islamic finance and its mode of operation is open and further developing. Some scholars claim the need for a Qur'anic based world-order to fully develop the idea of a purely real-economy-grounded financial system (Choudhury, 2007). On the contrary, practitioners like the head of the Association of Islamic Bankers in Kazakhstan, Yerlan Baitaulet, envision the establishment of Islamic finance as a further branch of modern ethical banking. Such disputes notwithstanding, a number of principles for the practice of Islamic finance have been confirmed over time. They are based on ideas of Islamic economics, a rather systemic body of rules for economic engagement in compliance with the Shari'a, and they all aim to contribute to the development of "asabiyya" (social cohesion) in society. Next to "zakat", a tax on wealth to provide for the needs of the poor and one of the five pillars of Islam, basic concepts in Islamic finance include the exclusion of "gharam", an excessive risk or uncertainty and related speculative action, and "riba", literally translated with "excess", "addition" or "interest" (Hakim, 2007). In Islamic finance, riba stands for the prohibition of interest on loans. Riba, or more correctly "usury" – as the term for specific financial interest – leads to "excess compensation without due consideration, and must be forbidden according to Shari'a law. Instead, Islamic economics proposes to counter the negative effects of such arrangements by balancing out losses and profits in business activities. This sharing of risks, called "mudarabah", is expected to contribute to a more just economy. Further principles resemble 5 the criteria developed in several branches of ethical banking, like the ban on investments into gambling or any other activity that must be considered "haram".

Of more importance are special forms of contracts that have been developed under Islamic finance and that today are used by Islamic banks and other Islamic financial institutions to circumvent the very strong economic incentive that interest plays in conventional banking. Following the general principle outlined above, as a contract form "mudarabah" is a profit- and loss-sharing agreement in which the bank provides financial capital, and the partner provides knowledge and skills. **"Murabaha"** is a form of a fiduciary sale, where the bank obtains a certain good and sells it to the buyer, the bank's client, with a profit. In such a transaction Islamic law demands that all information of costs in the transaction is being honestly declared and that it be rooted in real commodity trade, not only financial. The bank must buy the good, for example, a house, and sell it further to the buyer with the added margin. Another form of an Islamic financial operation is "musharakah", a joint venture in which parties agree in advance on profit sharing and where potential losses are divided according to the shares of the contribution made by each participant. Many more financial instruments have been developed for Islamic banking for example: "Sukuk" as a special Sharia conform bond, the Islamic lease "ijarah", or "bai salaam", a form of financing for deferred commodity exchange. In general, all financial instruments in Islamic banking aim to master the challenge to compensate for the time value of money in financial transactions without resorting to interest and yet guarantee the rooting of any transaction in the real economy.

Islamic name that basically runs on interest. Such discussions, as much as they are conducted among practitioners, scholars, and theologians, nevertheless matter for the expansion of Islamic finance and the development of Islamic banking practices in the countries of Central Asia. Uzbekistan and its neighbors are considered fertile ground for future successful Islamic business, yet they also demand new debates and efforts, like the establishment of Sharia councils, for instance, to define appropriate understandings of Islamic practices within their own societal contexts. For the most part, such considerations seem to be only in their initiation phase in all countries today, where the first institutional developments have been set off only in the last years.

SUKUK (ISLAMIC BONDS)

Sukuk is an interest-free bond that generates returns for investors based on the principles of Islamic Law. Unlike a conventional bondholder, a Sukuk holder is granted ownership in the asset or business being financed, and the return is tied to the performance of the underlying assets Sukuk has emerged as the second largest component of Islamic Finance which is gaining immense popularity and acceptance not only among the Muslim majority countries but also among the countries where Muslims are in minorities (COMCEC, 2018). Governments have started acknowledging the significance of Sukuk instruments, mainly in financing infrastructural development projects, and more started issuing Sukuk (mainly sovereign Sukuk) for financing their infrastructure development projects. For instance, in 2017, Nigeria issued its first Sovereign Sukuk amounting USD 277 million (COMCEC, 2018). The proceeds from this Sukuk issuance were used to finance the road construction and rehabilitation work. Additionally, a new class of Sukuk instruments termed “Green Sukuk” emerged whereby proceeds from the issuance of such Sukuk are channeled into environmental projects. A Green Sukuk is one of the most innovative Islamic finance instruments which support SDGs in the long run. Malaysia showed a leading role in socially responsible investing (SRI) and green finance, by introducing several initiatives to support the green agenda. The Securities Commission (SC) of Malaysia formulated the SRI Sukuk Framework in 2014 and issued the first green Sukuk in 2017. Through green finance Sukuk, the Malaysian government aimed to meet its target of generating 7,200 MW of renewable energy by 2020 (of which 2,080 MW is to be contributed by solar energy). In March 2018, the Indonesian government issued Green Sukuk worth USD 1.25 billion (Ramadan and Widenings, 2019) with the aim to fund the sustainable development of climate-oriented green projects. The issuance of green bonds increased globally to an aggregate value of approximately USD 258 billion in 2019 with green Sukuk accounting for USD 7.9 billion. The optimism surrounding green finance generally has extended to social financing which is likely to gain greater prominence as part of the COVID-19 recovery. In April 2020 the UNDP emphasized that Zakat and Sukuk can be used as a part of the pandemic response plan. Like its counterparts, Uzbekistan could also use Sukuk for raising funds to finance infrastructure, environmental, as well as commercial projects. However, Uzbekistan needs to establish a proper legal environment to enable the development of Islamic finance in the country.

1. The most important building block for the development of Islamic Finance is the legal framework which currently does not exist in Uzbekistan. To explicitly recognize Islamic Finance and banking in the legal framework, it is envisaged that a separate legislative act is enacted.

2. Regulations and Guidelines on Sukuk issuances shall be proposed in order to clear the confusion and even eliminate the inconsistencies, improve transparency and disclosures and crystallize the scope and mandate of Islamic Financial Institutions.

3. Implement international best practices and be at par with the latest global regulatory standards. One way is to adopt prudential standards and guidelines issued by the international standard settings bodies like AAOIFI, IFSB, and IIFM. The standards issued by AAOIFI shall be reviewed in light of local legal and regulatory frameworks and shall be adopted.

4. Select appropriate projects to finance through Sukuk and attract foreign investors. For example, in infrastructure or renewable energy.

5. Conducting job training by inviting industry people and sending candidates abroad for an internship in Islamic Finance and trading Islamic Securities in order to use these above-discussed Islamic financial contracts effectively in Uzbekistan, it is of utmost importance that Islamic financial laws coexist with the conventional financial laws. All matters pertaining to Islamic financial institutions should be dealt with by Islamic financial laws including dispute management.

PARTNERSHIP SPECIFIC ISLAMIC CONTRACTS

Musharakah: According to Usmani (1998) the term Musharakah in Arabic means sharing. The basic tenet of Musharakah contract is like a partnership contract in English law, wherein two or more partners come together to form an enterprise by pooling funds, materials, and intellectual property. Regarding profit and loss sharing, unlike modern partnership contracts, the profit rate is determined at the time of concluding a contract. The profit is shared among the partners based on the agreed profit rate. In case of loss incurred, each partner will share the loss according to the ratio of individual capital invested to the business. Mudarabah is a unique way of partnership facilitated in Islamic finance, wherein one partner provides all the funds required to start a business and the other partner invests those funds in a profitable venture through efficient and effective management. The fund provider is called Rabb al-mal (owner of the funds) and the manager of the funds is called *Mudarib*. The profit will be shared according to the pre-determined ratio agreed at the time of concluding the partnership contract, whereas in case of loss Rabb al-mal would have to bear all the loss.

THE STATUS OF THE ISLAMIC FINANCE SECTOR WITH ITS LEGISLATIVE FRAMEWORK IN UZBEKISTAN

The recent phenomenal growth in Islamic banking underpinned the need for greater innovation and flexibility to facilitate wider acceptance of Islamic products and services. The Islamic finance industry contains a number of institutions including commercial and investment banks, investment and insurance companies, e-commerce, asset managers, brokers, and dealers. Total assets of the Islamic finance industry grew by a CAGR of 6 percent to reach USD 2.44 trillion within 5 years from 2012 to 2017. Saudi Arabia, Iran, and Malaysia top the market with 65 percent (USD 1.6 trillion) share of Islamic finance assets. Among 56 countries, Nigeria, Cyprus, and Australia experienced the fastest growth in 2017. Banking is the main area of Islamic Finance contributing 71 percent or USD 1.72 trillion to the industry's assets with 41 countries having Islamic banking regulations. Commercial banking also remains the main contributor to the growth of the Islamic banking sector. This is due to the new openings of Islamic finance institutions in different countries. For instance, in recent years the Islamic finance industry has started to develop in CIS countries. Kazakhstan, Kyrgyzstan, Azerbaijan, and recently Tajikistan have established their Islamic banking regulations. However, Uzbekistan has not even begun the process of working on its legal framework. As a part of Uzbekistan's reforms aimed at attracting Muslim investors from other countries, the government started working on establishing Sharia compliant products including Sukuk and introducing the Islamic insurance sector. However, the Government has not achieved much progress in introducing the IF legal framework in the country, and this is hindering the development of the IF sector in the country. It is believed that if the Government agrees to step up its efforts, organizations like Is DB will extend their support in formulating a legal framework for the country and undertaking projects of various natures that will develop the IF industry.

TAJIKISTAN: A MARKET WITH PROMISES FOR ISLAMIC FINANCE

One would expect the Republic of Tajikistan to be an attractive place for Islamic forms of finance, considering the significant role Islam occupies in society. A short summary of macro indicators provides evidence to this claim: contrary to Kazakhstan or Kyrgyzstan, only a small percentage of non-Muslim minorities live in the country, making Tajikistan for most parts a Muslim society; the Islamic Renaissance Party the only Islamic party legally operating in Central Asia as of today, which makes Islam politically relevant in public life (Heathershaw & Roche, 2011); Tajikistan has strong connections to linguistically close Iran and seeks to broaden its relations to Pakistan, both nations with Islamic finance principles officially occupying a central place in the states' doctrines. Irrespective of such favorable indications, Islamic financing has been very poorly developed in Tajikistan. Like the other states in Central Asia, Tajikistan joined the Islamic Development Bank Group after independence, even if a bit later in 1996 for reasons of the ongoing civil war. Since then the country had received financial support to invest in infrastructural projects, especially power generation and transportation. According to some figures, 212 Mill. US$ were allocated to projects in the republic, other estimates count up to 500 Mill. US$ in funding for Tajikistan (DeCordier, 2012, & Trend, 2011). Further support was delivered by Islamic relief organizations from abroad to ease the burden of the civil war. The Saudi Arabian "Saudi Ali Gatha" and the Iranian *"Imdad"* both engaged in charitable activities and, according to De Cordier (2012), are still running projects in Tajikistan. The cooperation between Tajikistan and the IDB further developed in November 2011, when both sides signed an agreement on

Technical Assistance. This agreement foresaw the introduction of Islamic banking in the republic and pursued the goal to have the first institute operating by 2013. As of 2012, no registered Islamic finance institute was offering its services in Tajikistan. The legal framework has been under examination and changes to relevant laws have been discussed. In October 2012 the National Bank of Tajikistan signed an agreement with Zaid Ibrahim & Co, a Malaysian consulter and the biggest law firm in the Kingdom, to assist in drafting a law "On Islamic banking in the Republic of Tajikistan". With the political leadership expressing its interest in establishing Islamic finance institutes in the republic, some observers expected the first Islamic bank to emerge in 2013. Most likely this bank would be a "window" of an already established bank in Tajikistan since the market itself still is carrying too many risks for investors abroad. Efforts to spread Islamic finance instruments have been undertaken already for quite some time in Tajikistan. One driving force behind such initiatives so far has been the GIZ, the leading German development agency. In training and seminars with interested parties, among other staff from the National Bank, members of the "Association of Micro-Finance Institutes of Tajikistan", or representatives from governmental bodies, the GIZ was informed about Islamic principles of doing business and financing. In a conversation with the author, one expert told about some selected forms of Islamic financing already being practiced in Tajikistan. Especially depositing with micro crediting institutes was an instrument being tested in Tajikistan since 2011. This market entry for Islamic finance principles is reasonable considering the high number of micro-financing agencies operating in the republic. A report from 2010 counts 116 such agencies, dealing with depositing, loan-organizing and loan-funding and having more than 150.000 clients. Therefore, such structural advantages and the agreements for the further promotion of principles of Islamic financing will most likely contribute to improving conditions for the establishment of Islamic banking in Tajikistan in 16 the near future.

KYRGYZSTAN: EMERGING MARKET FOR ISLAMIC RETAIL BANKING AND ISLAMIC MICRO-FINANCING

Kyrgyzstan has been in the news and a subject of extended debates in political sciences for its unconventional developments in the last two decades. The often-chaotic events, with two revolutions in six years, swift changes from open to closed political regimes, and endless demonstrations and strikes, almost inevitably had their impact on the emergence of Islamic finance in the republic. Yet, parallel to the developments in Kazakhstan attempts to set up Islamic finance got a boost in the years 2008 and 2009. The history of Islamic finance in Kyrgyzstan is strongly connected with the Islamic Development Bank. The republic was the first country in Central Asia to join the IDB in 1993, following the liberal agenda of then president Askar Akaev. However, despite this early engagement, investments by the Bank in Kyrgyzstan have been the lowest among the Central Asian countries, amounting to only 159 Mill. US$ until mid-2012. For comparison, Kyrgyzstan is ranked third in EBRD investments; and holds the reputation to be a rather open country to foreign aid. The question for the reserved approach of the IDB notwithstanding, investments in recent years, since

2006, have been increasing. Most of the funding went into infrastructural projects, especially transportation, yet increasingly the support of a new system of Islamic banking was given priority. In June 2012 the IDB and the Kyrgyz government signed an agreement for technical assistance worth 193.000 US$ for "further development of Islamic financial services in the country". This new engagement in the facilitation of Islamic financing in the Kyrgyz Republic can be traced back to a memorandum, signed by the Kyrgyz government, the IDB, and the "*Ecobank",* a commercial bank operating in Kyrgyzstan in May 2006. This agreement owed much to the personal initiative of the head of the IDB in Kyrgyzstan back then, Shamil Murtazaliev, who laid out four steps for transforming Bishkek into an Islamic financial hub in Central Asia. It also opened the doors to new legislation which provided one of the most advanced legal regulation systems for Islamic financing business in the region in the following years (Osmonalieva, 2012; Aliyev, 2012, & Eurasianet, 2011). Following the memorandum president Bakiev, who had come to power after the ouster of Askar Akaev during the Tulip Revolution, signed a decree in July 2006 "On the Pilot Project of Introduction of Islamic Financing Principles in the Kyrgyz Republic". This decree enabled the National Bank of Kyrgyzstan to move forward with establishing new rules for Islamic finance institutes. Already in October 2006 the National Bank adopted a statute for Islamic financing principles, stating in detail conditions for Islamic banking instruments like *Mudarabah, ijara, Murabaha, "Sharika" (musharakah), or "istisna'a"* (deferred production sale). Finally, on 13 December 2006 the National Bank was entitled to hand out licensees to Islamic finance institutes operating in Kyrgyzstan. This leading role of the National Bank was further consolidated with two laws adopted by the parliament in March 2009 that made changes to the law "On the National Bank of the Kyrgyz Republic "and to the law "On banks and bank operations in the Kyrgyz Republic". Now the National Bank stipulated in Article 4 as one of its major functions the regulations of financial operations, including operations in line with the principles of Islamic banking. In addition, the bank had been entitled to formulate normative regulations to further organize the market for Islamic finance in the republic. In September 2009 the government took the decision to prepare the market for the introduction of Islamic securities in the form of Sukuk and takaful. Such groundbreaking work had its effects when government representatives in Kyrgyzstan concluded talks with consultants from the IDB and investors from Malaysia to set up an Islamic insurance company in the republic. To open up Islamic financing for the fast-growing microfinance sector in the republic the National Bank adopted further resolutions, allowing such institutes to offer micro-credit lines in the form of Mudarabah, musharakah, ijara, and others. The establishment of Islamic financial institutes in Kyrgyzstan was closely related to the stipulations of the memorandum in 2006. Not only was Murtazaliev head of the IDB; before he had acquired the former Kyrgyz branch of the Russian Credit Bank in 1997 and had it renamed Ecobank. Based on the memorandum, Ecobank became the first pilot project for Islamic banking in the republic and was eventually renamed Eco Islamic Bank in July 2010. Eco Islamic Bank provides a good case study for examining the opportunities and challenges to Islamic financing in the Kyrgyz Republic. Since 2007 the bank has been prospering, opening branches in all major cities across the country and gaining market shares. For 2011 the yearly audit revealed assets of more than 2,3 Bill. sum (48 Mill. US$) and reported a net profit of more than 60 Mill. sum (1,2 Mill. US$) (Marka Audit, Bishkek, 2012). Most of the deposit holders in Eco Islamic Bank are former clients of the branch of the Russian institute, yet the bank management was able not only to keep this mostly non-Muslim clientèle but to expand its base of customers. In 2010 the bank managed to sign 2.274 agreements with customers, in total worth 867 Mill. sum (19 million US$). Eco Islamic Bank is not only engaging in typical Islamic banking operations but also cares about the expansion of knowledge 14 connected with Islamic finance. It opened the educational center *"Barakat"*, where the bank trains future staff and invites cooperation. For example, in December 2009 representatives from financial institutes and supervisory bodies from Tajikistan visited Barakat to receive training in the principles of Islamic financing. Furthermore, and independent of *"Eco Islamic Bank"*, a small corporate investment firm, called *"Muslim"* started operating in March 2012 in Bishkek and two micro-credit institutes in Kyrgyzstan are handing out loans in compliance with Sharia law. In interviews with the author, representatives of the National Bank also confirmed that microcredit companies are testing the new regulations, with two firms, *"Companion invest"* and *"Kausar"* covering the South and the North of the country respectively. More firms were entering the market in 2011.Kyrgyzstan has proven a promising market for Islamic finance products, with 5% market share in the retail sector in 2012, and with predictions of 10%-12% in 2015, following here the generally positive development of Islamic banking on a global scale.

ISLAMIC FINANCE AND THE STATE IN CENTRAL ASIA

Summarizing the state of development of Islamic financing in the five Central Asian republics, some conclusions, even if preliminary at this stage of the research, can be drawn. To be clear, considering the gap in empirical research into informal practices of almsgiving and the works of Muslim charity organizations in the region, it is almost impossible to generalize about the relevance of ideas of Islamic finance, its principles like *asabiyya* or the prohibition of usury, to the population in the region. Also, the selected initiatives to establish banking institutes and micro-credit agencies do not add much to our knowledge due to their short existence. As of today, Central Asia is far from affording Islamic finance the importance and 19 corresponding institutional settings like those in the Muslim nations of the Persian Gulf, or in Iran, Pakistan, or Malaysia. Irrespective of that, the case studies allow us to hypothesize about the relationship between Islamic business practices and the state in Central Asia and therefore about economic action and state reaction in general in the region. In Kazakhstan, the central state is an important factor. Here lies the capacity to boost Islamic finance or to limit it to selected infrastructural projects. In interviews with experts the state is being identified as the key decision maker, yet, as the case studies show, also by means of initiative taking it holds the key position. The young history of Islamic finance in the republic tells of lobbyists, who concentrate their work on sound new legislation and who try to reach out to political decision-makers, and of private banks to wait for approval from the presidential administration. The central state in Kazakhstan makes the initiative to form commissions, invite experts from abroad, and supervise investment projects that carry the label Islamic. In sum, the central state distinguishes itself in Kazakhstan by its ability to control the development of Islamic banking. The absence of a developed retail market for Islamic finance, for example with *Al-Hilal Bank,* as well as the non-existence of microcredit agencies in this sector stays in contrast to the number of state organs involved in the process of Islamic finance evolution in Kazakhstan. The National Bank, the Financial Market Supervision Agency, the presidential administration, the Development Bank of Kazakhstan, and several ministries in recent years in various degrees participated in the preparation of new legislation as well as guiding and controlling the introduction of Islamic finance mechanisms into the market. Taking Islamic finance as an indicator, the central state's actions in Kazakhstan fit well into descriptions of a typical developmental state. In Kyrgyzstan, the central state less so than in Kazakhstan can take the attitude of obstruction but it is the condition for progressive developments in Islamic finance. Here the question of particular interest for the future is, to what extent the positive impulse can be sustained in the context of constant political changes. The challenge to Islamic finance expansion is to master changing political alliances and insecure state institutional settings. What was initiated due to personal relations between President Bakiev and banker Murtazaliev in 2006, and resulted in the National Bank becoming the driving regulatory force behind Islamic banking, so far has been only halfheartedly supported since the April revolution in 2010. Constant government dismissals represent the generally weak state in Kyrgyzstan and they carry the risk of a sudden change in personnel and the marginalization of supporting networks. However, Islamic finance seems not to rely solely on state support for its development in the republic. Initiatives mostly come from actors from non-government sectors. Banker Murtazaliev stands for a type of entrepreneur who calculates the risks of unstable state support against the open liberal economic context. In that sense, Eco Islamic Bank is the first example of privately organized Islamic banking in Central Asia and its followers are indicative of a favorable socio-economic context for doing Islamic business in Kyrgyzstan, against the background of a weak state and a chaotic institutional setting. Tajikistan seems to be in a position similar to that of Kyrgyzstan, yet some trends in Islamic finance development make the picture more complex. First, despite the advantageous condition of Muslim society, the initiative to establish Islamic finance institutes in the republic has been taken by development agencies and less so by entrepreneurs from within Tajik business circles. And second, disregarding the comparable stable context of the political regime in Tajikistan, the first steps to reform the corresponding legislation were made only very recently. In sum, in Tajikistan domestic actors seem rather hesitant to introduce Islamic banking. Since the institutional setting with concentrated decision-making power, developed relations with other Muslim countries, and experiences with micro-credit companies must be considered rather supportive, there is reason to believe that this caution is rooted in political considerations. In fact, Tajikistan's struggle against alleged Islamist groups, the competition of Rahmon's regime with the Islamic Renaissance Party, and the attempt to attract the big powers' attention feed a discourse that warns of an imminent Islamist threat (Schmitz & Wolters, 2012). Following this argument Islamic finance in Tajikistan falls victim to the extended employment of a discourse that serves regime stabilization in the first place but casts a general suspicion on any outright expressions of unconventional Islamic practices. Such political considerations certainly play a role in Uzbekistan too, but here a comparison to developments in Kazakhstan reveals considerably more insight. Both Uzbekistan and Turkmenistan created platforms to discuss Islamic finance and showed top-level commitment to international cooperation. This central state action shows the intention to benefit from the new relations with investors from Muslim countries. Yet it also discloses the weak control capacities of the central states in both republics, when such intentions do not translate into lasting reforms, into new market segments being made.

OPPORTUNITIES AND IMPEDIMENTS TO THE OPERATION OF ISLAMIC BANKS IN UZBEKISTAN

Bankers were given open-ended questions on how Islamic banks could contribute to economic development in Uzbekistan. 12 banks stated that Islamic banks would diversify funding sources and give interest-free loans to SMEs; Investment funds would be attracted from Muslim countries (from OIC member countries); the public would increase its confidence in banks; idle funds on hand of public and businesses would be invested in permissible *(halal)* projects/products through banks which will increase healthy competition among financial institutions and contribute to the GDP of the country; it will help to alleviate poverty by mobilizing funds appropriately; there will be justice in the financial transactions; literacy on Islamic finance products among public and bankers will also expand. Some banks also stated that according to their research 30 percent of the population does not use conventional banks' services due to religious reasons and they believe that if Islamic banks start operating here this gap will be narrowed down. According to an ADB study, 30% of the population did not use traditional banking loans due to their religious beliefs, and the opening of Islamic banks would fill this gap. Obstacles: Banks were also asked about the biggest obstacles and problems for the introduction of Islamic banking in Uzbekistan. The respondents stated the biggest problem was the lack of a legislative framework regulating Islamic finance products and services and that the current legislation of banking and taxation was not adapted for banks operating based on Islamic law principles. They also pointed out the inconsistency of local tax and banking legislation with the nature of Islamic finance operations, and the difficulty of processing Islamic products in the existing banking software systems. It was also recommended that the new legislation on Islamic banking and finance be made along with regulations covering Islamic insurance. Another obstacle that the country faces is insufficient expertise in the Islamic finance area. Suggestions by Banks: Banking legislation should be amended in a short period of time to establish Islamic banking and finance operations in Uzbekistan; Cooperation with developed countries and Islamic banks should be enhanced to attract international funding; AAOIFI-certificates to be introduced, and bankers in the field of Islamic banking and finance should be trained; Through the implementation of Islamic finance, the country will be able to introduce new types of financing instruments for the financial and banking sector, analyze foreign experience, reduce their shortcomings and risks, and effectively develop the sector in the short run. At the same time, the formation of partnership skills between the parties will be achieved. To introduce partnership-based or ethical (Islamic) financing in the Republic of Uzbekistan, it is necessary to form a corresponding legal and regulatory framework which, in turn, will allow the country to receive additional capital and offer alternative financing mechanisms to the population.

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