



The Role of Islamic Banking in Financing Small and Medium-Sized Enterprises

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Abstract

Islamic banks play a pivotal role in financing Small and Medium Enterprises (SMEs) by providing a Sharia-compliant financial alternative that avoids interest-based loans. Their approach is characterized by utilizing diverse, risk-sharing financing modes such as Mudaraba (profit-sharing), Musharaka (partnership), Murabaha (cost-plus sale), and Ijarah (leasing). The role of Islamic finance extends beyond pure economics to encompass social and sustainable developmental dimensions, fostering social solidarity through instruments like Zakat and Waqf. Empirical evidence from various countries indicates that Islamic banks are more engaged in aggregate SME lending and generate more revenue from servicing them compared to conventional banks.

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1. Introduction

An Islamic bank is a financial institution that mobilizes and deploys funds within the framework of Sharia. Its purpose is to advance development across social, economic, environmental, and related dimensions. In the Islamic conception, economic development proceeds in tandem with social, urban, cultural, and environmental development; the aim is to produce a balance among diverse determinants and orientations.

From this perspective, development is grounded in the premise that the human being is a vicegerent on earth, entrusted with its cultivation in accordance with God's law and ultimately accountable in the hereafter, as conveyed in the Qur'anic verse: "Then We made you successors on earth after them, so that We might see how you act."¹

Islamic thought articulates this mandate through the notion of 'imāra/ta'mīr (cultivation), a term used to denote what is essentially sustainable development, as reflected in: "He brought you forth from the earth and settled you upon it; so, seek His forgiveness, then turn to Him in repentance. Indeed, my Lord is near, responsive."² The sense is that people are made builders of the earth. The scope of 'imāra exceeds the conventional economic definition of development and extends to the breadth of human life. In this vein, Imam 'Alī ibn Abī Ṭālib advised his governor in Egypt: "Let your attention to the cultivation of the land outweigh your attention to extracting revenue, for revenue is realized only through cultivation; whoever seeks revenue without cultivation ruins the country." Islamic political economy therefore aims to foster a community in which individuals, acting in God-consciousness, pursue the earth's cultivation, safeguard the attendant blessings and resources, and adhere to divine law so as to secure a sufficiency level for all and sustain growth over time.

Globally, small and medium-sized enterprises (SMEs) have acquired an elevated status because of their central role in market economies; they often function as a barometer of national strength or weakness. Finance is fundamental to these firms, yet it is also among their most acute challenges—particularly at the start-up stage. Many SMEs rely on bank borrowing, and the interest burden becomes an added constraint.

Financing is thus essential for the establishment, operation, and expansion of SMEs. It covers ordinary working needs and underpins continuity. For this reason, the development of financing instruments has drawn sustained attention from financiers and investors.

This study therefore asks: What role does Islamic banking play in financing SMEs? To address this question, the analysis proceeds as follows:

- Section One: Characteristics of Islamic banking in financing.

- Section Two: Intermediation in Islamic banking as a vehicle for SME finance.
- Section Three: Islamic financing modes for SMEs.

Section One: Characteristics of Islamic Banking in Financing

Contemporary scholars of Islamic political economy have examined how Islamic banks contribute to sustainable development, emphasizing effectiveness both in theory and in practice. Their conclusions challenge the premises of conventional (non-Islamic) finance on efficiency, performance, and technical advancement. This is most evident in credit and financing, where the prohibition of *ribā* and the application of partnership-based and trade-based contracts—*mushāraka* (equity partnership), *muḍāraba* (trust-based profit-sharing), and *murābaḥa* (cost-plus sale)—operate as modern instruments that, in many settings, mobilize savings and channel them into productive investment more effectively than interest-based banking.

Islamic banks are comparatively better positioned to invest available resources by sharing in decision-making and bearing responsibility for outcomes. The partnership principle enhances macro-stability, while the breadth of contracts—*muḍāraba*, *salam* (forward purchase), *muzāraʿa* (sharecropping), *istisnāʿ* (commissioned manufacture), and *mughārasa* (tree-planting share arrangement)—provides suitable vehicles for financing capital-intensive projects associated with sustainable development³. By design, Islamic banks are developmental: they mobilize domestic resources and savings and allocate them to economic, social, and environmental projects that yield goods and services of demonstrable public benefit⁴. Their purpose therefore extends beyond profit-seeking to the pursuit of shared welfare between fund suppliers and users⁵.

Islamic banks also carry a particular responsibility for advancing *ʿimāra*—the constructive cultivation of the earth—given their stewardship over financial resources. Developmental by nature, the Islamic bank combats hoarding, pools savings, and directs them toward investment in ways consistent with the *Sharīʿa*, thereby serving society through an institution that is at once economic, social, financial, and banking. Its mission is to restore money to its foundational social function

Islamic financing exhibits several distinctive traits⁶. Chief among them is that funding is structured without a pre-profit “cost” understood as a deduction from gross revenue prior to profit determination; under Islamic modes, the investor’s net gain is not reduced by an interest charge. In addition, funds are available through multiple contractual forms rather than exclusively through credit (loans), as in conventional banking. In practice, Islamic banks employ *muḍāraba*, *mushāraka*, lease-to-own and sale-leaseback variants, *salam*, and *murābaḥa*. Such arrangements temper individual self-interest—on both the financier and entrepreneur sides—because each party receives

a return proportionate to its contribution to value creation within a sustainable-development horizon. Profits, when realized, are allocated according to a pre-agreed ratio among all contributing parties; conversely, losses are apportioned among them in line with the risk-sharing terms of the contract.⁷

A further hallmark is the coupling of economic with social development, a linkage without which economic gains do not translate into broader welfare. Through its investment policy, the Islamic bank seeks to raise living standards and widen access to livelihoods by supporting productive enterprises. Grounded in Sharī'a—which upholds the preservation of life and human dignity—the Islamic bank also institutionalizes social solidarity in the deployment of funds. Economic activity, in this perspective, forms part of worship: a means to uplift the material and spiritual dimensions of life in service of a higher purpose⁸.

Interest in Islamic banking has grown alongside policy attention to small and medium-sized enterprises (SMEs). Islamic banks have achieved notable results in both Muslim-majority and other jurisdictions, whether through direct financing or indirectly via financial intermediation. The following sections address each pathway in turn.

Section Two: Intermediation in Islamic banking as a vehicle for SME finance

The core function of banking institutions is financial intermediation between savers and small and medium-sized enterprises (SMEs). In the Islamic model, this intermediation establishes the criteria for bank finance, mobilizes idle funds, and deploys Sharī'a-compliant investment methods—eschewing interest-bearing loans used by conventional commercial banks. Direct transactions between individual savers and SMEs are, in practice, hindered by divergent preferences regarding liquidity and risk. Intermediation resolves this mismatch. On the liability side, the Islamic bank first mobilizes savings in the form of deposits, zakāt, and waqf resources.

1) Deposits⁹

a) Demand deposits. These are repayable on call at the depositor's request. The bank guarantees their repayment and manages them under its responsibility and in the depositor's ownership; in effect, the bank bears the liability for any loss.

b) Savings (time) deposits. In the conventional system, these are typically larger in volume, placed for an agreed term, and early withdrawal forfeits the depositor's expected return. In Islamic banking, this category is invested and its proceeds shared with depositors under a lawful muḍāraba arrangement. As a pool, such savings tend to be longer-dated—even when some placements are individually short-term—thereby providing the Islamic bank with a principal source of funding for financing and investment operations.

In addition, zakāt and waqf can play an active role within intermediation: the Islamic bank may collect zakāt and channel it to its lawful outlets, receive endowments from donors, register applications from eligible recipients, review them, and disburse accordingly.

2) Zakāt

For present purposes, zakāt may be defined as a compulsory financial due collected by the state—or its delegated public bodies or individuals—on a non-quid-pro-quo basis, assessed according to the taxpayer's ability to pay, and allocated to the eight categories specified in the Qur'ān, in line with the requirements of Islamic public policy.¹⁰

Historically, zakāt has been a recognized revenue of the Islamic state. In contemporary practice, the Islamic bank can gather zakāt and redistribute it to eligible recipients. As a pillar of social solidarity, zakāt has proven to be a reliable source for meeting the needs of the poor and providing for the incapacitated. Classical experience shows that systematic collection and disbursement helped curb poverty and deprivation to the extent that, at times, there were no eligible claimants upon the public treasury¹¹. Operationally, centralized collection and targeted spending allow the Islamic bank to influence the circulation of money—expanding or restraining it. When excess liquidity is observed, zakāt can be directed to local outlets; when contraction is required, allocations may be routed to the public treasury (Bayt al-Māl)¹².

Zakāt addresses one of development's chief constraints: insufficient funds available to extend to entrepreneurs, itself a corollary of low per-capita income¹³. It also contributes to the ethical and social order by fostering a community of justice, solidarity, and reciprocity. By redistributing wealth, zakāt increases monetary circulation across society—production, consumption, and welfare alike. Economically, it effects a reallocation of income and wealth and stimulates investment and national income. The mechanism is straightforward: a known share is transferred from the affluent to the poor—from those whose marginal utility of money is low to those for whom it is high—thereby boosting effective demand for goods and services, raising aggregate consumption, expanding productive capacity, and, in turn, increasing national income and investment¹⁴.

Assets subject to zakāt must be: fully owned, productive or capable of growth, above the niṣāb (threshold), in excess of basic needs, free of net debt, and held for one lunar year¹⁵.

Zakāt links the three core dimensions of sustainable development¹⁶ as follows:

- **Economic:** Zakāt is the Islamic system's primary distributive instrument. To ensure continuity and precision in its application, it is constituted as a pillar of religion rather than left to shifting economic decisions, social contingencies, or personal whims. As a stable, recurring right

in wealth—payable upon meeting its conditions—zakāt undergirds ongoing production of goods and services and helps preserve macro-balance between aggregate output and public debt.

- **Environmental:** A system that is environmentally sustainable preserves a stable base of natural resources, avoids excessive depletion of both renewable and non-renewable assets, and safeguards material and biological resources¹⁷.

- **Social:** Zakāt purifies the giver from miserliness, habituates Muslims to spending in the path of God, and cultivates the character of the affluent. It binds society through solidarity and fraternity, combats poverty, ignorance, and disease, and propels the economy forward by enabling the poor to access work opportunities and means of production¹⁸. Zakāt also supports Qur’ān institutes and religious universities, underwrites students in need, advances literacy, counters deviant doctrines and harmful ideas, and provides a livelihood safety net for families. In short, it is a high form of social insurance unmatched in historical experience, extending tangible assistance to persons with special needs and to low-income households¹⁹.

Waqf (Endowment)

Waqf was known among the Babylonians, ancient Egyptians, Romans, and Germanic peoples. Over time, the idea evolved from being confined to religious institutions to encompassing a wide range of charitable and developmental bodies. Many legal systems developed arrangements analogous to waqf. The Anglo-American Trust closely resembles it, and French civil law contains several dispositive acts that operate in a similar fashion. With the advent of Islam—and in step with the rise of Islamic civilization—the institution of waqf expanded markedly, producing a vast legacy of endowments for worship, learning, social care, and public utilities²⁰.

Ibn Qudāma al-Ḥanbalī defined waqf succinctly as “locking the corpus and dedicating the yield.” The definition signals a perpetual charity in which the income from the endowed asset is continuously spent on one or more lawful purposes. For more than fourteen centuries, Muslim societies have relied on waqf as a moral and economic base for building civil institutions and sustaining them in scientific, educational, health, and service fields. This tradition delivered durable forms of sustainable development—education, health, environmental upkeep, and community services. Modern Arab-Islamic societies inherited many civil institutions established and preserved through waqf: schools, public libraries, health and social care facilities, public water fountains, and other amenities woven into the social fabric²¹.

Environmental protection occupies a high position within the maqāṣid al-sharī‘a. Safeguarding the environment upholds two of life’s necessities: the protection of life and the protection of property. Sharī‘a imposes a duty to preserve both, and the means necessary to fulfill

that duty take on the ruling of obligation, since “what is necessary to perform an obligation is itself obligatory.” Environmental waqf therefore counts among the pious works commended by the law. Benefactors and endowers should direct attention and resources to this crucial facility and steward its initiatives wisely²².

Islamic banks can operationalize waqf by deploying Sharī‘a-compliant investment modes as follows:²³

1. Substitution (istibdāl). The endowed asset—movable or immovable—may be sold for cash, with the proceeds used to purchase a replacement asset that is then made waqf in lieu of the original. Properly executed, istibdāl can position the waqf to play a more effective role in financing small and medium-sized enterprises.

2. Leasing the waqf (ijāra). This is among the most common investment forms and gives the waqf administration greater flexibility to restart or reconfigure investment activity, including transitions from leasing to other modes. Lessee uses are constrained to what serves the waqf’s interest. A practical structure is for the waqf administration to grant SMEs the use of endowed land to develop an investment project. Once built, the investor operates the project for a defined term and pays a periodic consideration to the waqf. At term’s end, the land and superstructures revert to the waqf for subsequent exploitation as deemed appropriate.

3. Partnership (mushāraka). The Islamic bank, acting as owner or manager of waqf assets, may enter partnerships with other investors, either as a regular equity partner, as a muḍārib (entrepreneur under a profit-sharing contract), or in a hybrid arrangement. Profits are distributed among contributors according to their agreed shares.

4. Agricultural financing. Depending on the nature of the endowed land, the bank can apply mughārasa (tree-planting share arrangement) and musāqāt (crop-sharing for orchard care and irrigation). The agricultural output is divided between the waqf and the investor at a ratio agreed in advance.

Section Three: Direct Financing in Islamic Banks

Islamic finance exhibits distinctive features²⁴. Chief among them is that funding is structured without a pre-profit “cost,” understood as an amount deducted from revenue prior to profit determination. This structure can allow the Muslim investor to retain a larger net profit than under interest-based credit. It also offers multiple contractual forms, unlike conventional banking which relies primarily on bank credit (loans). In practice, Islamic banks finance through muḍāraba (trust-based profit-sharing), mushāraka (equity partnership), ijāra arrangements (including lease-to-own and sale-leaseback variants), salam (forward purchase), and murābaḥa (cost-plus sale). Bank

financing in this model tempers individual self-interest—whether on the financier’s side or the entrepreneur’s—because each party receives a return proportionate to its contribution to value creation within a sustainable-development horizon. When profit materializes, it is distributed among all contributing parties according to their pre-agreed ratios; when loss occurs, it is apportioned in line with the contract’s risk-sharing terms. A further hallmark is purposive allocation: funds are directed to investments with social benefit, a central asset of Islamic finance in sustainable development. Evaluation typically draws on expertise from several parties whose interests are tied to the venture, which improves the project’s prospects and reduces failure risk.

Forms of Direct Islamic Financing

1) Muḍāraba (Trust-based Profit-Sharing)

Muḍāraba is one of the principal financing modes in Islamic political economy and underpins the core banking idea of accepting deposits and investing them. It is a profit-and-loss sharing arrangement in which one party provides capital and the other provides labor and management. Depositors (as capital providers) supply funds; the bank invests those funds in projects that benefit society on the basis of a common share in profit, while the entrepreneur supplies effort and skill. Beyond its private benefits, muḍāraba supports the creation of new enterprises, generates employment opportunities, and helps mitigate unemployment²⁵.

In classical jurisprudence, muḍāraba arises when the capital owner entrusts funds to an agent—merchant, craftsman, or worker—to trade with them. Profit is shared as agreed; loss falls on capital alone unless negligence or misconduct by the agent is proven. Article 621 of the Jordanian Civil Code defines the muḍāraba partnership as a contract whereby the capital owner agrees to provide funds and the muḍārib to exert effort and work in pursuit of profit. In banking practice, muḍāraba means the Islamic bank enters a specific transaction with one or more counterparties, the bank providing capital and the counterparty providing effort. Both share gain and risk. The bank is the capital partner; the counterparty is the managing partner (muḍārib). Profits are distributed per the agreed ratios; capital loss, if any, is borne by the bank, and the muḍārib loses only his effort—unless negligence or transgression is established. The use of muḍāraba is historically attested before and after the advent of the Prophet, and it was not repudiated²⁶.

Advantages of muḍāraba financing

- Commercial and investment advantages: Muḍāraba integrates the two primary factors of production—capital and labor—and supports efficient resource allocation. It expands real productive projects, generates and raises incomes, helps counter recessionary tendencies, increases national income by mobilizing financial and human resources, and reaches small farmers, producers, and investors.

- Social advantages: It alleviates unemployment by creating new jobs through new ventures; it yields a fair distribution of returns between capital owner and muḍārib; it increases the number of proprietors as some wage earners become owners; it supports a more balanced social structure.

2) Mushāraka (Equity Partnership)

Mushāraka is a foundational mode for Islamic banks. The bank is not merely a financier but a partner; its relationship with clients is partner-to-partner, not creditor-to-debtor²⁷. Two or more parties jointly finance a project and co-own it. Since a bank's core function is financing rather than indefinite ownership, diminishing mushāraka is frequently used: the Islamic bank enters as a partner, contributes equity, enjoys the rights and assumes the obligations of a partner, and an agreed mechanism governs the bank's gradual exit through sale of its shares to the other partner(s). Mushāraka does not add to a project's financial cost in the manner of interest, and it incentivizes all parties to ensure success because they share outcomes. Risk is borne jointly in fair proportion to contributed capital and as stipulated for profit-sharing²⁸.

3) Ijāra (Leasing / Lease-to-Own)

Also termed lease-based sale structures, ijāra is suited to financing fixed capital. It typically begins as a lease of machinery or equipment and may end in transfer of title if the investor opts to acquire the asset²⁹. Legally, it is the transfer of a permissible usufruct for a known period in exchange for consideration; in effect, a sale of benefits. As a banking service, ijāra is a developed alternative to conventional asset finance. It matches the funding needs of producers seeking cutting-edge productive equipment and, at the same time, serves entrepreneurs who wish to renew capital assets by renting them with periodic installments calibrated to their repayment capacity.³⁰

4) Istisnā' (Commissioned Manufacture/Construction)

Istisnā' is a contract by which one purchases, at present, an item to be manufactured by the seller with the seller's own materials, to specified descriptions and within a defined time. In contemporary usage, it is a Sharia-compliant financing technique: a procurement agreement to make and deliver what will be manufactured in accordance with agreed specifications³¹. Ḥusnī 'Alī Khuraywesh defines it as "a contract for making a specified thing as a liability, and it is among the contracts of sale." The International Islamic Fiqh Academy (OIC) states: "The istisnā' contract—

being a contract pertaining to work and to an object held as a liability—is binding on both parties if its pillars and conditions are satisfied.” In practice, *istisnāʿ* has enabled Islamic banks, in jurisdictions that apply it, to deliver significant volumes of residential, investment, and industrial construction; the largest share by value has been in real estate³².

5) Islamic Securitization (Sukūk)

Islamic securitization is the conversion of Sharia-acceptable assets into financial certificates (*sukūk*) whose patrimony is segregated from that of the originator and which are tradable in a financial market, provided their subject matter consists predominantly of tangible assets. These certificates have defined maturities and an undetermined return *ex ante*; they carry risk. In substance, the process is a division of ownership in assets and financial holdings into units, each represented by a tradable certificate for investment in capital markets under Shariʿa standards. Unlike conventional securitization, which is typically debt-based and relies on credit enhancements, Islamic securitization is asset-based: the relationship is not one of creditor and debtor but one of co-ownership in assets and entitlement to profit or exposure to loss.

Within Islamic banks, *sukūk* support sustainable development and investment by supplying medium- and long-term funding, thereby helping to rebalance bank balance sheets through the placement of deposited funds into long-dated investment certificates. A bank may finance projects across sectors and then issue financing and investment *sukūk* specific to those activities³³. Islamic *sukūk* also address liquidity constraints—an essential driver of economic activity—as observed in global crises where liquidity dried up and banks and firms failed. This experience prompted major economies (including, for example, the organized French market) to adopt Islamic *sukūk* frameworks. Because issuance must be backed by identifiable assets and returns arise from profit rather than interest, *sukūk* can contribute to a healthier alignment between the real economy and financial flows³⁴.

Islamic securitization can raise market efficiency by curbing fraud, unfair dealing, and destructive speculation that redirect resources toward purely rent-seeking activities, distort price discovery, and unsettle overall price levels. In contrast, Islamic *sukūk* mobilize financial resources toward real investment while dampening speculative pressures. They also drive the development of Islamic capital markets by widening and deepening those markets with new instruments and by catalyzing ancillary financial institutions integral to this architecture³⁵.

A further feature is risk prudence: anchored in Shariʿa principles that prohibit gambling and excessive uncertainty, *sukūk* structures offer risk-mitigating characteristics that can reassure funders and investors regarding their property interests—without eliminating commercial risk³⁶. Many Muslim-majority and other countries now apply this mode of financing³⁷.

6) Murābaḥa (Cost-Plus Sale)

Murābaḥa is the most widely used investment mode in Islamic banking due to its relatively lower risk³⁸. It is a sale at cost plus a disclosed profit. When the price is paid immediately, it functions as a straightforward sale: the buyer takes possession and pays in full. When the price is deferred—lump sum or installments—it functions as financing. Banks employ murābaḥa to fund purchases of fixed assets, raw materials, tools, and office supplies³⁹. As a sale of trust (buyū‘ al-amāna), its validity requires that the Islamic bank first acquire title to the goods in a manner customary in the relevant market. Title transfer mechanics vary: an individual purchasing a tangible item typically inspects the goods, whereas a trader importing merchandise may rely on shipment documents. In all cases, the bank remains bound by the agreed terms and bears the risk of damage, defect, loss at sea, fire, and similar perils until risk passes according to the contract⁴⁰.

7) Salam (Advance Purchase with Deferred Delivery)

Salam is a forward sale of a specified, fungible good—described precisely—against an immediate cash price, with delivery at a known future date⁴¹. It is the inverse of a conventional credit sale: the price is paid now; the good is delivered later. The seller (muslam ilayh) obtains the liquidity required to finance operations and repays in kind by delivering the stipulated commodity at the agreed time. Properly designed, salam can moderate prices—thereby easing inflationary pressures—while enabling the investor to obtain funds without an interest cost⁴².

8) Tawarruq (Cash Monetization via Commodity Trades)

Tawarruq secures cash by purchasing a commodity on deferred terms and then selling it to a party other than the original seller for spot cash⁴³. Banking practice often uses “organized tawarruq”: the bank arranges the purchase of a commodity—commonly from international commodity markets—on a deferred-price basis for the client seeking cash, and, by term of the contract or commercial custom, undertakes (as the client’s agent) to sell the commodity to a different buyer for spot consideration and to remit the proceeds to the client⁴⁴.

9) Agricultural Modes: Muzāra‘a, Musāqāt, and Mughārasa

- Muzāra‘a: the landowner grants land to a farmer to cultivate or work; the crop is shared between them by prior agreement.
- Musāqāt: a contract to tend existing trees or plants (irrigation, care, harvesting) in return for a share of the yield.
- Mughārasa: the land is granted for a known term on condition that the worker plants trees; the resulting trees and produce are shared as agreed⁴⁵.

Conclusion

This study yields a set of findings and recommendations.

Findings

- Islamic banks seek to mobilize savings and provide services and investment operations on Sharī‘a-permitted bases, with the aim of delivering social, economic, and developmental outcomes.
- In their transactions, Islamic banks employ Sharī‘a contracts and financing modes such as murābaḥa, muḍāraba, mushāraka, ijāra, salam, istiṣnā‘, and tawarruq.
- Zakāt and waqf play a significant role in sustainable development by channeling finance to small and medium-sized enterprises (SMEs).
- Strengthening waqf for environmental protection requires concerted legislative, institutional, research, and financing efforts.
- Islamic banks and financial institutions offer suitable instruments not only for SMEs but also for large enterprises.
- Islamic financial institutions provide financing that is responsive to the specific requirements of SMEs.
- SME financing enhances the operational effectiveness of Islamic banks and Islamic financial institutions.
- Islamic financial institutions seek to balance the preferences and objectives of all stakeholders; like other economic entities, they pursue efficiency by directing funds toward income-generating, lower-risk investments, often at the expense of riskier alternatives.
- Non-profit vehicles—especially zakāt and waqf—tend to finance projects with higher returns and lower risk in order to preserve funds while serving vulnerable groups.
- Islamic banks and Islamic financial institutions are capable of offering a Sharī‘a-compliant alternative to interest-based finance, which is associated with a range of prohibitions and objections.
- Financing is not the only constraint facing SMEs. In Algeria, the state has provided substantial funding across sectors; however, an unfavorable investment climate led many firms to be liquidated at an early stage.

- Support mechanisms have often been administered in an ad hoc manner: sizeable sums went to projects lacking financial and marketing feasibility studies, producing saturation in certain activities and, consequently, numerous bankruptcies.
- Given the high-risk surrounding SME activity, all financial institutions—including Islamic ones—require personal and real (collateral) guarantees, a practice that sits uneasily with the normative model of Shari‘a-compliant banking.
- Many financing requests fail because project sponsors lack basic information about their operations, maintain no accounting records, and cannot supply the documentation that banks require—particularly economic feasibility analyses.
- Beyond guarantees, Islamic financial institutions undertake in-depth financial, economic, and marketing feasibility studies to assess the capacity of projects to generate profit, expand, and remain viable. They often dedicate specialized units to this task and rely on experienced professional staff.

Recommendations

- Treat waqf and zakāt as core funding resources for Islamic banks and deploy them to develop projects that realize ‘imāra (the constructive cultivation of the earth), stewardship, and corporate social responsibility.
- Ensure strict application of Shari‘a rules across all banking operations, while innovating new financing structures that remain fully compliant.
- Improve the investment climate for Islamic banking—policy support, enabling regulation, and practical facilitation—to advance sustainable development.
- Raise banking literacy among public officials, society at large, and Islamic-bank employees so that the distinctiveness of Islamic banking vis-à-vis conventional banking, and the quality of its services, are clearly understood.
- Organize training courses, seminars, and workshops for current staff and for those establishing Islamic banks, with a view to deepening expertise in Islamic products and services.
- Leverage Algeria’s diverse endowments—across sectors—to catalyze the desired economic take-off led by SMEs.

- To avoid wasting substantial funds without meeting policy goals, overhaul the governance of support mechanisms and adopt a national coordination plan among all agencies that sets out support modalities and specifies eligible activities.

- Expand the scope of Islamic banks and Islamic financial institutions; where appropriate, design new institutions capable of performing similar roles at lower cost.

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