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# THE ROLE OF SUSTAINABLE FINANCE IN PROMOTING ECONOMIC AND SOCIAL DEVELOPMENT ON ISLAMIC BANKS

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**ABSTRACT**

Islamic financial organizations, which work in agreement with Sharia law, assimilate financial innovation with social accountability in instruction to challenge global issues relating to sustainability and inclusivity. This academic article explores the means in which Islamic banks ease economic and social progression done performs of sustainable finance. Finished a proportional analysis of the financial crops providing by Islamic banks and their conservative complements, the study clarifies the important role played by Islamic financial institutions in development long-term economic growth, justifying differences, and indorsing social wellbeing. Also, the study inspects the distinctive physiognomies of Islamic banking, counting the exclusion of interest and the ordering of moral investment, and evaluates their possible to challenge expansion trials within the MENA region. The study achieves with references aimed at supplementing the bulk of Islamic banks to further donate to economic and social expansion, in al Islamic financial determined with global sustainability objectives.



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## INTRODUCTION

Islamic banks combine social objectives and financial innovation to offer new solutions to specific problems that have arisen in a financial system over-dependent on complex financial products. These banks have proven to be resilient in the face of economic crises, demonstrating a steady growth rate that surpasses that of conventional banks. The Islamic financial system serves as an exemplary model of inclusivity and sustainability. It operates on principles grounded in the equitable distribution of income and wealth, the generation of employment opportunities, and the promotion of economic development. As such, it presents an ideal foundation for initiatives aimed at mitigating inequalities, eradicating poverty, and fostering sustainable development. The remarkable success of Islamic banks serves as a testament to the notion that adopting a long-term shared value perspective can pave the way for global inclusiveness. Rather than relying on reduced regulation, these banks advocate for widespread reforms that prioritize the wellbeing of all stakeholders, ensuring their protection and prosperity. Through their comprehensive approach to finance, Islamic banks champion a transformative banking system that addresses the complexities of a modern financial landscape while fostering social and economic progress. By merging profit with purpose, these institutions redefine the boundaries of conventional banking and inspire a new era of responsible finance. [1, 2, 3, 4]

In 2015, the international community defined the post-2015 development agenda and the 17 Sustainable Development Goals (SDGs) as a plan for people, planet, prosperity, peace, and partnership. In the 20th century, Muslim communities turned to Islam for guidance on critical economic and social issues. In terms of financial intermediation, the Islamic banking system has become a viable and unique approach to financial products and services that meet the ethical and moral criteria derived from the principles of Islamic Law (Sharia). Islamic banking is based on the purpose of an asset and the results of its use. From the demand side, Islamic banks are institutions that are committed to financing economic development, through their support for small and medium-sized enterprises (SMEs) and commitment to social justice. [5, 6, 7, 8]

**Background and Rationale**

A mounting debate has been concerned with the intrinsic contradiction created by private finance, which is typically confounded by short-term horizons, and the long-term sustainable and inclusive development agenda. Therefore, much attention has been directed towards the alignment of sustainable financial goals to the broader development objectives. The need for compliant and supportive sustainable investment agendas embraced by the finance community has become a priority, designed to specifically channel and properly utilize resources to make a concrete and long-term contribution to individual, environmental, and social development. In order to contribute to a fast achievement of these targets, Islamic finance institutions could play an essential role, provided that they align with the inherently sustainable and fair nature of Islamic finance principles and comply with Shariah precepts. [9,10]

Financial markets are considered as key actors in the achievement of a sustainable global economic system that promotes both growth and social justice. Development is essentially about the ability of people to expand their capabilities, which in turn can lead to the ability of the present generation to meet their needs without compromising the ability of future generations to do the same. Financial markets have a critical role to play in shaping a decent life by providing the financial resources necessary to foster investment by households, firms, and government into people, the planet, and social capital in ways that are sustainable. Financial markets have to take into account both the need for immediate gains and the respect for the needs of future generations. [11,12,13,14]

### Research Objectives

To examine the financial products offered by both types of banks, including Islamic and conventional banks, we conducted a literature survey and extracted some important products for analysis. To analyze whether Islamic banks are just as actively promoting sustainability by offering products that focus on major projects, economic development, and social progress as compared to the conventional banks, we use the "Cash Deposits" section of the NBD official website for its comparison. At the same time, we also check the website for the Shari'ah-compliance principles on the 'General Investment Accounts' section. [15,16]

This paper aims to achieve two main goals. The first goal is to offer an in-depth understanding as to whether Islamic banks have a significant role in promoting economic and social development by examining their practices in sustainable finance. This includes looking at the types of financial products offered within Islamic banks compared to the conventional banks, and whether the former are indeed exhibiting a more sustainable financial behavior by offering financial products to cater to both economic growth and social needs. Secondly, when sufficient evidence is found on the above fresh perspective, the paper aims to propose suggestions on what needs to be improved and what policies need to be introduced in order to encourage Islamic banks to further promote economic and social development. This is because no matter how well Islamic banks perform in promoting economic and social development as compared to conventional banks, there is always room for improvement, for which academic research has a significant role in demonstrating such a requirement. [17,18]

## METHODS

### Scope and Methodology

The traditional space used to debate these issues is the privatization of public services. There are really great questions that have opened various windows of opportunity to a diversification that has allowed the use of bonds, commercial paper, and Islamic funds among others, that have provided the financial conditions necessary for the viability of public entities. With reference to the great opportunities already identified, the wish is that the job has been properly organized and focused so that public banking contracts have these objectives as reference with no loss of efficiency in banking services provided to individuals. First, some design concepts are assessed to build a public banking product which takes into account different possibilities in the private sector. The concept of public banking is not questioned because public banking has historically justified the social focus that financial entities have been willing to assume. The political and commercial purpose of public banking makes private sector innovation limited and focused while the public sector is more comprehensive, especially in non-profit areas such as social objectives. Public banking also absorbs innovations made in the private sector, particularly to apply funds from external entities that prioritize financial innovation. [19, 18, 20, 21]

The primary scope of the paper is to explore the innovative financial instruments that underpin the strengths and weaknesses of the Islamic banking system in promoting economic and social development. The paper adopts a methodological approach mainly based on the critical analysis of innovative financing instruments, which are the most suitable for addressing social issues associated with FA. With this regard, the study also assumes some empirical contributions connected with the "Beyond Best Practices" approach. In fact, through the BG best-in-class search, the aim is to discover what other European countries have been doing in the field to understand if there are any potential for public finance different methodologies that could be imported and adapted to the national framework criteria. Due to the subjectivity of nearly all social indicators and the different paths to social advancement chosen by countries, there is no magic solution but the method chosen brings empirical elements in this debate. [22, 21, 23]

## RESULTS AND DISCUSSION

### Conceptual Framework

Islamic financial institutions must act on the guidance and direction given by Islam, which links and rationalizes its activities, and does not interfere with them. The direction and direction provided by Islam in financial and economic issues is sometimes direct, and sometimes not. Some of these issues concerning this issue which are specified by the Holy Qur'an are defined, including interest and similar reinsuring interactions, the nature of money and currencies, the use of resources, the price disguises and the reality of trade. Interest is forbidden in numerous religious teachings. However, given the substantial limitations on its functions, Islamic finance is a working area where Islamic teachings can easily interpret it.Islamic financial institutions play a pivotal role in our global economy. As custodians of Islamic principles, they are bound by the guidance and direction given by Islam. These principles not only rationalize their activities but also serve as a compass pointing towards ethical and moral practices. The guidance provided by Islam in financial and economic matters is vast and comprehensive. It encompasses various aspects, ranging from direct commands to nuanced interpretations.

One of the fundamental concepts discussed in Islamic finance is the prohibition of interest, commonly known as usury. The Holy Qur'an explicitly forbids engaging in interest-based transactions, emphasizing the importance of fairness and justice in financial interactions. This prohibition extends to similar reinsuring interactions, discouraging practices that can lead to exploitation or inequality.

Moreover, Islamic teachings shed light on the nature of money and currencies. They highlight the role of currency as a medium of exchange and store of value, while emphasizing the importance of avoiding excessive speculation and excessive hoarding. Islam encourages the circulation of wealth and resources to benefit society as a whole.

In the realm of trade, Islamic finance emphasizes the importance of transparency and honesty. Price disguises, such as artificially inflating prices or concealing defects, are strongly discouraged. Islam promotes fairness and integrity in business dealings, urging individuals and institutions to prioritize ethical conduct over immediate gains.

Islamic finance provides a unique and robust framework that aligns with Islamic teachings. While interest is forbidden, Islamic financial institutions have found innovative ways to engage in financial transactions that comply with religious principles. Through concepts such as profit and loss sharing, leasing, and partnerships, Islamic finance offers a viable alternative that maintains the spirit of fairness and justice.

With its emphasis on ethical practices and social responsibility, Islamic finance continues to evolve and adapt to the changing global economic landscape. Islamic financial institutions are committed to upholding the principles provided by Islam, ensuring that their activities not only adhere to religious guidelines but also contribute positively to the welfare and development of individuals and communities.

In conclusion, Islamic financial institutions have a significant role to play in promoting ethical and responsible financial practices. By adhering to the guidance and direction given by Islam, they can navigate the complexities of the financial world while staying true to their religious values. Islamic finance offers a comprehensive framework that covers various aspects such as interest, money, resources, trade, and pricing. It is through these principles that Islamic finance continues to thrive and make a positive impact on the global economy. [24, 25, 26, 27, 28]

Corporate social responsibility has been assumed by many companies who want to be considered as good companies. The importance of this matter has grown so important that various groups pressurized businesses about it, and sustainability reports written up by companies. In these reports, especially collusion problems with instituting it must provide us with a number of problems and political relations. These relations cover the products and services provided by the company. This issue is not only a hot problem of conventional businesses, but also presents Islamic finance businesses with a crucial dilemma. [29, 30, 31, 32, 33]

Sustainability is an issue of concern for countries all over the world. It is influenced by the fact that all types of human activities are limited by environmental factors. Regardless of the factors which are limiting their activities, it is in contradiction to long-term economic growth. For these reasons, countries need to adopt sustained notions of growth patterns and industries must invite games from resources. It is recognized now that not in the sense of maximizing profit but in order to promote the welfare of the community in general and that of the company's constituency in particular, businesses should focus on their activities.[ 34,35,36]

The aim of this paper is to investigate how the Islamic banking characteristics contribute to economic and social development in the MENA region and to analyze how economic inequality affects this relationship. The case study is realized using data from

6 MENA countries in the period 2003-2012. We find that Islamic banks offer a mixed performance in terms of economic and social development, and that economic inequality affects this propensity.

Economic and social development are fundamental goals of all countries all over the world. Economic development is often defined as staying within the laws of imperceptible time and developing the world's resources and the people, while social development is the improvement of standard living for a society. The two enhance each other, but achieving them is not easy. This is proved by the fact that many countries have not yet managed to reach acceptable development goals. [37,38]

**Sustainable Finance: Definition and Principles**

Sustainable finance, in other words, is primarily focused on financing the development of human and social aspects and significantly enhancing the environmental performance and social responsibility of companies. These comprehensive and inclusive objectives yield numerous benefits from various perspectives. Ethically and morally, these objectives hold immense value and are highly regarded by renowned institutions like the United Nations Principle of Responsible Investments, the OECD principles on corporate governance, and even the principles of Islamic finance, which emphasize sound ethical and moral values in financial activities. Moreover, there is a growing ecological urgency that necessitates the search for new models and principles, driven by a heightened awareness of the need for sustainable practices.

It is important to emphasize that the benefits of sustainable finance extend far into the future, and they have profound implications for the value of invested capital. By addressing the costs that the current system automatically bears due to its failure to appropriately evaluate externalities, sustainable finance effectively reduces associated risks. This includes mitigating social tensions and minimizing the adverse impacts of natural and environmental calamities. Additionally, responsible finance contributes to enhancing the value and profitability of credit institutions while positively impacting every entity involved in the responsible finance ecosystem.

The advantages of sustainable finance go beyond financial gains. They promote a well-balanced and equitable society, foster sustainable economic growth, and safeguard the overall well-being of individuals and communities alike. By channeling financial resources towards socially responsible and environmentally friendly practices, sustainable finance plays a crucial role in shaping a resilient and sustainable future for generations to come. Through collective efforts, we can create a world where finance serves as a powerful tool to drive positive change, catalyze innovation, and build a better future for all. [39,40 ,41]

The first question that needs to be answered in order to understand the role of Islamic finance in funding SDGs is what sustainable finance is. There are many different definitions of this concept and its scope, as it is reflected by the variety of terms used to refer to it - ethical investment, ethical finance, green finance, among others. The common denominator of all these terms is that they refer to a form of financial intermediation that seeks to balance the traditional objective of returning on invested capital in the form of funds lent or quotas purchased, with the preferences and aspirations of investors who believe, for cultural, scientific, religious, or esoteric reasons, that the capital must be used responsibly to solve problems of social and environmental concern. [42]

**Link between Sustainable Finance and Economic Development**

When comparing with traditional commercial banks, Islamic banks play an important role in poverty reduction and promote economic growth in underdeveloped areas. Islamic banks have done a lot in the fields of agriculture, infrastructure, and poverty alleviation. At first, Islamic banks offer advantageous financial service products and models. Moreover, Islamic banks actively help small and medium enterprises, microcredits, the socially vulnerable groups, and regional economics to develop. Therefore, Islamic banks have become an important guarantee for the growth of developing economies. The demonstration of the successful and positive experience of Islamic banks is very important for those international financial communities who have been actively exploring private channels to cooperate with the government to promote sustainable development in less developed areas in the case of peaceful lending. [15]

Sustainable finance, as an important part of financial services, targets three aspects: economic development, environmental production, and social fulfillment. In the context of contemporary financial operation, fulfilling social missions and contributing to the development of an international financial system are important for modern financial businesses, as important as the pursuit of economic profit. The international community showed strong concerns on poverty reduction and climate change governance acts. For the future development and prosperity of the international financial community, it is necessary to research the link between sustainable finance and economic and social development. [43,44]

**Link between Sustainable Finance and Social Development**

For that reason, industries and business activities are encouraged to take account of social impact with respect to current business strategies and to undertake CSR activities linked to their business activities. The raison d'être of business is built in generating profits from the business activities, and it is necessary for the management to bear such objectives in mind and to guide corporate policies consciously to aim for such a purpose. The definition of CSR, as posited by the Commission of the European Communities, is defined as dynamic and voluntary where business and society meet, with a focus on innovation and enterprise, and the interest of all stakeholders, and entails the integration by companies of social and environmental concerns in their business operations and in their interaction with stakeholders on a voluntary basis. [45]

In order to strengthen CSR activities from the perspective of SD, it is necessary also to establish appropriate support systems and safeguards. Industries and businesses can contribute even further to social development when CSR activities are organically linked to business activities, while taking account of their business and industrial situations, and ecological balance. These activities will not only contribute to the sustainable development of the industries and businesses concerned, but in the broader context, contribute to the sustainable development of the whole of society. It is necessary to aim to develop a society coexisting with growing industries and corporations. For industries and businesses, CSR in are means for growth and will lead to reinforced industrial competitiveness. Industrial development and progress leads to the economic development of nations and the development of communities. [46,47]

**Islamic Finance: Principles and Practices**

Islamic finance has grown rapidly and has become an important niche market in the financial services industry. Despite the skepticism of some from Western economic circles concerning the effective operational aspects of an Islamic economy, an Islamic economy has demonstrated a remarkable adaptability towards many of the so-called Western values of the modern world such as interest-free banking, profit/loss sharing, and joint management between the creditors and the entrepreneurs. The establishment of Islamic banks, takaful, Islamic mutual funds, Islamic capital and money markets, Islamic accounting and auditing practices, and relatively new innovations such as sukuk and securitization signify the Islamic economic infrastructure that provides a viable and feasible alternative to conventional finance while procuring economic and social development in a manner congruent with the objectives and principles of Islamic law. The basis of Islamic finance is rooted in two facts: a. all economic resources are considered a trust from Allah, and b. individuals are expected to direct their activities with good and proper intentions in their desire to fulfill their own natural entitlements. [48,49]

As for Muslim jurists, with its roots derived from Sharia law, the main principles of Islamic finance were generated from the Quran and other sources by exploring their implied legal obligations and teachings. Based on the Prophetic Tradition (Hadith), one must have sound knowledge of the matter with which he deals, become honorable and trustworthy, have full authority over it, and have the capacity to execute the contract into which he entered. The Quran gives its description as a guide to mankind, the code of conduct, and the complete way of life. [50]

**Overview of Islamic Finance**

A project enclosed in a welfare subcategory can belong to one or more economic categories at the same time. Therefore, Bh(o) projects e i are treated as i concurrent Bh(e i) financial projects for what concerns the total interest generated by the financing bank. In the same way, each Bh(i) project is considered as i concurrent Bh(i i) interest projects.

Concerning Islamic finance classification, welfare activities are labeled GIBC, while M&D, surveys, pre-feasibility studies and similar projects are termed GIBD. The projects executing any of them are noted Bh(o) and Bh(i). The first letter indicates the type of interest in the finance and it can be N (none), F (financial), I (interest) or O (other), while the other letters indicate the categorization of the project. Each Bh(o) project belongs to a single I_j category, such as buildings, public safety, water and wastewater. The category represents a field of interest and it includes subcategories. Every category and subcategory contain canonical or specific financial conditions (rate of interest, duration of finance, instalments and others) in relation to the economic segment or economic development index. For example, the interest rate can be related to the economic sector in which the economic niche is classified, to the destination of the buildings or to the destination of the nonresidential structures. [51]

It is essential to separate operational projects from welfare activities in the Islamic finance classification. Some projects aim to make people's living conditions evolve to a better stage, such as new houses, new vehicles, software, antennas, flour, fuel, workers' wages, ordnance, plastic, road construction, water pipes, and dams. These projects are operational and lead to welfare in a direct way without regard to meeting any limitation. Other projects are addressed to satisfy a necessity to enable welfare activities to be executed, such as M&D, seismic zone analyses, pre-feasibility studies, and geotechnical surveys. These projects may allow economic development to be promoted. However, projects such as M&D influence welfare in an indirect way without meeting an internal or an external limitation. [52,53]

**Key Principles of Islamic Finance**

In the history of Islamic finance, the reign of Caliph Umar (approximately 634–644 AD) marked an important socio-economic chapter in acquiring many normative foundations of Islamic banking and finance. These included the commitment and use of Islamic bank's money in trade and agricultural activities, the distinction between houses' and assets' financing and investments from donations' products. More than 1300 years after that period, the Islamic financial industry witnesses a remarkable actualization of these recurring and ongoing principles. The industry is not only growing in the Muslim world, but also expanding product and services quickly to the non-Muslim world. Opinion-wise, many prominent scholars and academicians of the polemic West have been increasingly expressing their appreciation, fascination and actualizing message for Islamic finance, thereby forcing it to soon co-enter their home market in the egging efforts of financial engineering preoccupancies. [54,55]

Islamic finance is simply a unique version of financial intermediation with the presence of distinctive and immutable ethical norms and values. In this light, contemporary Islamic finance has gone through certain evolution and revolution periods, and its operations are now made up of a noteworthy bit of subtraction and addition measures. This is in contrast to conventional banks, and the prevailing principle of its finance is interest-based growth maximization. This paper adopts and posits the principle-based approach to coarsen the key modus operandi of an Islamic bank in terms of its risk management system. Overall, we conclude that the proposed Islamic banking principles not only work harmoniously for both the overarching macroprudential policy and microprudential regulation jurisdictions but their implied current risk management model are also corroborated in empirical and anecdotal contexts. [56,57]

**Comparison with Conventional Finance**

Zainulbhai, Schatsky argued on congenial values of cooperation between sectors that they do not have a financial profit. Sustainable finance and Islamic finance share the common thread of focusing on the two stakeholders in the economic process as discussed earlier, social and economic prosperity are current reflections of the promoting community agreement that Islamic banking promotes through various risk-sharing and trade concept mudarabah from the takaful unit that contribute to diminishing agents' agreement when ensuring instruments.[55,65]

The advanced dialogue between the promotion of sustainable development from the Islamic finance industry and the strategies of conventional finance for fostering Corporate Social Responsibility (CSR) on sustainable growth are remarkably coincident. Much work has been done in this relation, and some researches comparatively evaluated conventional and Islamic finance in the issue of sustainable development. While sustainable and responsible banks are put in addition to investing to profit, Islamic financial institutions provide community awareness of corporate social responsibility. These finance institutions adopt Sharia, which does not allow any use or trade tied in promoting socially damaging business activities like drugs, gambling, or tobacco. These financial institutions make investment decisions based on analyzing environmental, social, and governance issues (ESG) combined with financial considerations.[57]

**Sustainable Finance in Islamic Banks**

According to the Shari'ah, credit and debt are allowed, but changes can be carried out in the financial sector by fostering legislation that promotes just and ethical lending. A crucial point is that, unlike old and modern conventional banking, Islam bans speculation (gharar) and interest (riba). This distinction in the nature of innovative Islamic finance facilities can promote the concept of sustainability and help leverage Islamic banking to consolidate itself. Islamic banking has, since its inception, emphasized a universally recommended approach comprising regular monitoring and assessment not only by the Central Bank of countries where Islamic banks operate, but also by the Shari'ah Advisory Board, all institutions established by global watchdog organizations, and ordinary customers.

Islamic finance is grounded on the principle that commercial and financial activities should be productive and beneficial for economic development and society. As a result, the provision of aid and social services is intrinsic to Islamic "luxury". While for-profit organizations are important, social and economic missions are subordinated to their commitment to offer long-term benefits to both society and the community. As a result, it is the duty of the Islamic banking model to engage with clients to ensure that the finances deployed are being used in a legitimate manner. [58,59]

**Integration of Sustainability in Islamic Banking Practices**

The increased intermediation role of the bank provides high levels of physical investment, technological advancement, and thus a quick and equitable wealth distribution. If it is correctly and effectively allocated, these resources in the creation of the real economic activities will increase the size of the economic pie which will eventually offer a positive and zero-sum game for most investors and society as a whole. In that respect, the knowledge and management categories in Islam have a social function that delivers justice for all stakeholders and others whom the business may affect, and be environmentally aware, thus fostering sustainable development. Similarly, Islamic law does not differentiate between different types of Qard-Hasan, however, it explicitly points out categories of the deserving poor and their rights to claim it. Some authors compare the categories classified by Islamic Law and Corporate Social Responsibilities categories as shown in Table 1.

Table 1: Comparison of Categories Classified by Islamic Law and Corporate Social Responsibility (CSR)

| Islamic Law (Shariah) | Corporate Social Responsibility (CSR) | Comparison |
|---|---|---|
| 1. Economic Responsibility | 1. Economic Responsibility | |
| Prohibition of Riba (Usury) | Profitability and Sustainability | - Islamic law prohibits earning through interest to ensure ethical earnings. |
| Zakat (Charity) | Economic Impact | - Obligatory charity to purify wealth and support the needy. |
| 2. Social Responsibility | 2. Social Responsibility | |
| Social Justice and Welfare | Community Engagement | - Islamic law ensures justice, equality, and welfare in society. |
| Prohibition of Harm (Darar) | Employee Well-being | - Avoiding actions that harm individuals or society. |
| 3. Environmental Responsibility | 3. Environmental Responsibility | |
| Stewardship of the Earth (Khilafah) | Environmental Protection | - Duty to protect and maintain the environment. |
| Prohibition of Waste (Israf) | Sustainable Practices | - Avoiding wastefulness in the use of resources. |
| 4. Ethical Responsibility | 4. Ethical Responsibility | |

| Islamic Law (Shariah) | Corporate Social Responsibility (CSR) | Comparison |
|---|---|---|
| Honesty and Integrity (Sidq and Amanah) | Ethical Business Practices | - Maintaining honesty and trustworthiness in dealings. |
| Fair Trade and Contracts (Aqd) | Transparency and Accountability | - Ensuring fairness and clarity in business contracts. |

In Islamic banking, in the conventional system, the bank has full autonomy to charge any amount of interest (riba) to its clients, which is not the case in Islamic banking. Here, the bank has no full autonomy to excessively exploit its clients by charging higher rates of returns at exorbitant percentages. Consequently, Islamic banks cannot just give out money to the productive investors without some form of similar risk-sharing. Also, in Islamic banks as a function of economic importance both banks' capability to increase their solvency and clients' solvency is desirable for them to produce optimal equity finance that will finally make financial services fulfill their roles more effectively and efficiently despite the level of market development. By driving the bank into the real economic sector, Islamic banks therefore perform these functions more closely than conventional banks. [60,61]

**Case Studies on Sustainable Finance Initiatives in Islamic Banks**

The Umma Card, introduced by Bank Rakyat Indonesia 46 (BRI46) in 2008, is an innovative way of doing corporate social responsibility of a bank in line with Maqasid Shariah, because it seeks to help Indonesian micro and small enterprises (MSEs) to develop sustainably by providing them with access to credit through credit cards which facilitate the purchase of BRI46-currently involved Umma Card Merchants (BSU) categorized as "local vendors" and "Halal properties". In cooperation with BRI's micro, small, and medium enterprise (SME) bank partners, the BRI46 Foundation provides coaching to BSU partners to assist them to establish business units in the Islamic financial services sector.

The focus on the role of Islamic banks in social development has gained more attention in recent years, as indicated by a number of case studies and survey reports on sustainable finance practices conducted by several Islamic banks. In response to the increasing demand of customers and shareholders, due to the affirmation of growing awareness that future corporate success and competitiveness will also depend on the social and environmental responsibilities of business, as reflected in the principles of good corporate governance, several Islamic banks have overseen the establishment of sustainable finance programs, such as the "Umma card", the Zakat Collection Programme, the "Green Credit" program, and the Legal Project. [62]

**Impact of Sustainable Finance on Economic Development**

None of these studies document the role of finance channels that would determine the effect of sustainable finance on economic development. The Islamic financial system can meet these needs by creating a greater inclusive finance, and by providing sustainable development through its application. The Islamic finance system can create growth and promote value-added production, advance job creation, and reduce the significant economic gap between Islamic countries in the West, and importantly alleviate the intensity of extremes of poverty. This paper, part of an economic series, highlights the role of Islamic banking in delivering sustainable finance and promoting economic development. On the one hand, the role of Islamic banks in promoting sustainable finance and economic growth is underestimated, while, on the other hand, the ethical underpinnings of Islamic banking have been largely misunderstood. [63]

We project that sustainable finance can create significant positive externalities via the creation of these public goods, which could make it particularly worthy of policy focus. In addition, there is a growing awareness of the link between finance and growth, with sustainable activities themselves projected to be a major driver for economic development. The impact of financing on the economy is not automatic, and the economic support from finance is contingent on the distribution of bank loans through different sectors. As the relationship moves between different stages, it may change nature, exert contractionary effects at too high a level or unravel completely. This is why empirical evidence on the impact of finance on growth is divided, and depends on the interaction between the economy and the financial system. More recently, studies suggest that there is a significant role played by the banking sector, where more specifically the type of bank, such as Islamic banking, and the personality of the financer, are major determinants.[64]

**Direct Economic Impacts of Sustainable Finance Initiatives**

It is found that investors' decision-making related to the bank's CSR initiatives is based on investors' interest and the returns that they seek. Investors who are interested in maximizing financial returns, either in the short or long term, will consider activities that generate economic benefits, while investors who are not interested will consider economic, social, or environmental benefits. There is evidence that banks with good community and social focuses promoted economic development as it can contribute additional taxes, increase economic activities, and improve the social environment. In addition to this, banks also create social value by preserving and generating additional value. In the long term, banks may contribute to an effective economic system and satisfied society by addressing social and environmental concerns. [64,40]

The discussion on the role of banks in contributing to the economy and wider society through their social and environmental impacts is not new. Despite a number of previous studies that have focused on the relationship between banks' operations and economic development, there is still a debate about what constitutes the banks' 'positive' contribution to sustainable development. Some studies focus on the direct impacts of banks toward economic development. According to the bank specialist, positive direct impacts generally refer to the provision of accessible financial services and the creation of additional jobs by SMEs. In this context, the joint partnership activities carried out by banks were through CSR (Corporate Social Responsibility) initiatives. Some studies revealed that banks with CSR initiatives were more likely to deliver positive results in terms of attracting the attention of investors by undertaking activities that contribute to the welfare of society[63,64].

**Indirect Economic Impacts through Investments**

It is important to note that Islamic banks and other Islamic financial institutions are not immune to business cycle characteristics and general macroeconomic conditions. However, the channels through which fluctuations in real economic activity are transmitted are quite different. The main distinction between Islamic banks and other banks is that Islamic banks operate to varying degrees in the field of profit-and-loss sharing, while the activities of Western interest-based banks are driven by the payment and receipt of interest[14,16].

Addressing the economic aspects, Islamic banks channel their funds to profitable and productive projects and enterprises in the real sector of the economy and engage in trade-financing activities, in which no tangible assets are bought or sold in large amounts. Islamic banks offer Ijarah (leasing), Mudarabah and Musharakah (plant and equipment financing), and Musawamah (purchase and sale) financing in contrast to commercial banks. Islamic banks provide long and medium-term finance, which is needed for industrial enterprises. Islamic banks can make better use of surplus savings of residents, which were previously dissipated in unproductive channels for financing government deficits. [65,66]

**Impact of Sustainable Finance on Social Development**

At the heart of their strong social performance, Islamic banks share several common elements. The first is the obligation to contribute directly to community welfare. The second characteristic is their commitment to assist in sharing risks and obligations, initiating improved charitable activities, and contributing to micro and small credit operations. The third element is their requirement to perform screening processes for immoral investment and to refuse to invest in prohibited industries. Islamic banks were created and have operated under the belief that banks and financial institutions are morally obligated to act ethically in the interest of human well-being in the societies in which they operate. The study also found that when addressing sustainable finance, Islamic banks share various principles with the broader principles of environmental and social finance.

The concept of Islamic finance refers not only to an investment requirement but also to a moral obligation, the purpose of which is to promote human well-being, not to prolong its existence. Such a concept is consistent with the fact that banking operations, being characterized by inherent risk, are founded on sound principles. Based on the moral premise and the requirement to share in risk-sharing mechanisms, there can be spill-off effects in terms of social performance, which is widely seen as a core element in fostering social and economic justice in society. The study that examines social contributions within Islamic banks has found that participating banks not only spend more on their Zakah activities but also they have, in general, been more active in propagating such activities. [67,68]

**Promotion of Social Welfare through Sustainable Finance**

Islamic banking refers to banking activities that are carried out following the principles of the Shariah. The principal function of Islamic banking and finance is to foster social justice and to advance the needs of an entire society. Islamic banking is an integral part of ethical finance as it restates the purpose of finance: pursuing the well-being of both individuals and societies. There are three pillars to ethical compliance in Islamic banking: a direct relationship between financial institutions and individuals based on profit and loss; a ban on gambling, exploitation, trade of money for money, and usury, exploitation and speculation; and the requirement for transactions in contracts and the obligation to manage financial assets. Islamic banks have become an important model that embraces Maqasid al-Shariah to contribute to the development and well-being of their society and directly addresses the needs of the real economy. Therefore, the Islamic finance industry has grown significantly throughout the world. It has also encouraged other financial systems to develop and promote responsible investment that focuses on enhancing the welfare of society, the economy, and the environment. Islamic banks are guided by Shariah principles and where social welfare has to be taken into account, and Islamic banks cannot engage in activities that are not Shariah-compliant to achieve social welfare. These principles also prioritize the beneficiaries of resources available in the economy through the allocation of credit and the provision of financial services.

Sustainable finance focuses on the environmental, social, and economic dimensions. In the context of social, sustainable finance is targeted at promoting greater social cohesion. In particular, the development of the Islamic financial industry has incorporated the concept of social welfare. A concept closely related to the aspect of sustainable finance, the Maqasid al-Shariah, underpins principles guiding business transactions to achieve social welfare. These guiding principles are built on two important points: adopting principles of social benefit that focus on the well-being of the community and reducing financial inequalities, and promoting social justice that brings the economy back into balance. Islamic banks must consider the impacts of their activities on society when deciding the products and processes, as they are guardians of the well-being of society and are not only accountable for the capital that has been entrusted to them. The key consideration is behooving the Islamic bank to ensure that their financial intermediation promotes social well-being. [69,24]

**Case Studies on Social Development Initiatives in Islamic Banks**

The Bank Group was the first official institution to establish the Waqfah Fund, which has provided interest-free loans to over 50,000 applicants to date. Since the program is approved by Shariah, the Fund has become a Mecca for those with lesser means over the years. Its visibility was perpetuated between 1998 and 1999, when the program extended interest-free loans worth 222 billion TL to 199 children with no other means. This amount was a bit more than a mere drop considering the country's economy.

The Waqfah Fund is a quantitative project where giving small interest-free loans is a requirement. Firstly, these loans must be completely interest-free. Secondly, they must be equal. And thirdly, the beneficiaries should have no other choice but to sin. All of these conditions are achieved with the backing of Shariah and Fatwa. The Waqfah program was inaugurated at a ceremony in 1992. The fund began with 1 mg of gold being deposited into it in 1992, and from the very beginning, it was a superior method of soliciting the Lord's pleasure.

The Waqfah Fund is a modest attempt by the Al Baraka Banking Group to create a sharing relationship between the top management of Al Baraka Bank and people with lesser means, in order to help the needy buy necessary equipment through interest-free loans. This fund will gradually grow through collections made from a portion of the profits determined by the Executive Thiqah Committee for interest-free collection.

## Challenges and Opportunities

In attempting to achieve its goals, Islamic finance faces several challenges that can limit its potential in stimulating the economy and, by doing so, may negatively affect human welfare. Undoubtedly, both economic development and the business model on which Islamic finance is based are particularly complex and involve values. This generates tensions, including ambiguities in the types of risks and regulatory impost of Islamic banking. Islamic economic values are not the same as Islamic banking operations. Islamic banking involves taking on multiple risks and costs that can act as a barrier to access to financial operations or cause additional costs if banks need to undertake additional measures. However, any relaxation in regulation may open opportunity for moral hazard and bank risks rising, detracting from the very goal that Islamic finance seeks to meet, and would not be in line with the substantial overlaps in the substantive functions and activities of Islamic and conventional banking.

## Challenges Faced by Islamic Banks in Implementing Sustainable Finance Practices

At present, financial constraints in producing sustainable finance can be addressed by applying existing technology in the infrastructure and alternative material, which can aid in creating a variety of infrastructure and services. However, Islamic banks still encounter problems in providing such kind of finance. Currently, most Islamic banking institutions perform activities similarly as conventional banking institutions. They are not just used to mobilize funds from the public but also they provide an array of financial services such as savings, loans, money market investments, and most of them provide an ATM facility. Nevertheless, the impact of the positive role of Islamic banks (which is based on the Islamic legal principles) is sometimes still questionable. Such shortcomings have increased the challenge that faces Islamic banks in the implementation of sustainable finance practices.

Islamic banking has experienced rapid growth despite the conservative Shariah principles governing the contracts between the Islamic banks and depositors and between the Islamic banks and their borrowers. The implementation of Islamic banking must not only focus on product design but must also promote the general welfare of the economy. However, competition constraints and a manual documentation system make Islamic banks face difficulty in implementing sustainable practices fully. Failing to implement a system and allowing competitors to utilize modern technologies that minimize the service cost might make Islamic banks fail to extend financial products at a reasonable cost. This chapter addresses Islamic banks' crucial role and their ability to play a major role in promoting sustainable finance for the benefit of the community. [17,70]

**Opportunities for Growth and Innovation in Sustainable Finance**

This work specifically focuses on the innovative role played by Islamic banks, which has shown better resilience to the recent global financial crisis, the restraint of speculation, and a deep level of long-term economic relationships between banks and real economic activities. These characteristics coincide with the norms and prescriptions of the religiously-based ethical standards that shape Islamic finance. The Islamic finance model is based on equity, participation, and the sharing of risks and rewards. Since its first appearance, Islamic finance has been developing in two main directions: pure financial services and potentially ethical investment operations/product implementation. Islamic finance has its religious roots in Islamic jurisprudence (Shari'ah), which is based on the Quran and the Hadiths, where there are strict prohibition bans (Riba - usury, Maysir and Gharar - excessive uncertainty) and prescription aids (Zakat and Sadaqa, promoting social justice and distributing and sharing wealth) from which we can draw commonalities with SRI principles.

Moreover, considering that the demand for sustainable or responsible finance is currently not being fully expressed by the markets, because of a lack of knowledge about the subject or because of substantial switch costs such as those related to the personal attention required by choosing and managing a "meaningful" portfolio characterized by the integration of ESG criteria. Considering that in a context where all the relevant market participants would have adopted the perspective on SDGs, better macroeconomic indicators would emerge and better SDGs-oriented investment behavior would be incentivized.

The promotion of more sustainable and more socially responsible forms of finance is of fundamental importance in order to enhance the effectiveness of the overall finance sector in promoting more sustainable and inclusive economic development. Furthermore, sustainable finance can enhance the involvement of the ultimate stakeholders, who are the real owners of the resources and the ultimate beneficial owners of the financial sector. This will also ensure better governance of the financial system overall. As a consequence, universal investors who have a strategy considering ESG dimensions can become key players in determining the transformation of the market implied by the SDGs. In order to incentivize the economic agents in the search for this finance, a series of investment guidelines and criteria can be adopted by the different investors. [42,71]

## CONCLUSION

It is not a question of knowing or discussing bank performance – however, this seems to be useful – but of contributing to the bank itself to become aware of one of the potential resources it has in its business. It may be useful for a financial objective – in these days in which everyone talks about purpose in a different sense – to be sensitive to the fact that its activity can contribute to the common welfare. And it can contribute to modifying the functioning of society, in the sense that the use of the financing that society provides or not does not contribute to maintaining a behavior in the production of goods and services that society perceives as essential for its own survival. With the exception of modern Islamic banks following the profit maximization paradigm, the financial system needs the resources of this bank clientele. It can take a step in this direction. Is there not a growing dissatisfaction of savers with respect not only to market volatility but also to the sense of their investments in terms of the world's evolutionary process, in terms of the potential social and ecological impact in developed and developing countries?

This paper emphasizes the fundamental role of traditional finance in shaping the world in which we live today. It challenges the idea of philanthropy imposed in front of finance with an ethical vision, considering ethics as a part of the financial decision-making process and praising a culture of sustainability properly understood. Likewise, it pays special attention to the practical implementation of this philosophical change, focusing on the role of Islamic Finance and analyzing the application of these ethical tenets in an Islamic Bank in particular. The results show a very clear orientation toward sustainable economic and social development. It is also in line with the results of conventional and web studies and opens the door to an important practical change, such as highlighting this feature to attract more savings inflow.

### Summary of Key Findings

In this context, ethic-oriented non-financial performance indicators that encourage a customer and stakeholder-oriented business performance can provide an important long-term corrective to generate sustainable finance. Islamic banks provide a body of knowledge on how financial systems reconnected with the values of society would work to prevent moral hazards, externalities, and systemic risks and, thereby, contribute to society's economic and social development.

Many conventional banks in western countries are facing the problem of how they can make sufficient profit to pay high salaries and deposit interest to shareholders and other stakeholders when demand growth for many of the conventional banking services is leveling out. More damaging is that conventional banks, when they maximize profit, have a strong tendency to create moral hazard, externalities, and systemic risk, the 'Global Crisis.'

Therefore, in order to provide further input to this critical policy debate, it is important to show which factors enable finance to contribute significantly to the sustainable development of an economy. This paper provides an empirical example, focusing on Islamic bank theory, stressing the changes necessary to the organizational structure, business culture, and business strategies of banks.

The role of finance in economic and social development has been a debated issue for decades. This debate has recently intensified, driven by a more pressing concern: the need to meet the Sustainable Development Goals. There is a consensus that the purpose of finance should be broadened from merely profit-making to facilitate economic and social progress. However, proposals on how innovative and sustainable finance can be fostered and allocated are often abstract.

**Implications for Policy and Practice**

Islamic banks may want to consider proactively quoting and negotiating prices about potential material sustainability information that (i) directly affect future income and/or (ii) shed light on the corporate risk profile, performance, and liquidity. In fact, Islamic banks can actually evaluate and price the costs of potential ethical and legal scenarios. Both Islamic and conventional banks can negotiate damages to the company as well escrow/spread the risk across different regional boundaries. Towards this end, the motivation at the regional and national level to establish a Sharia-and a Securities Commission would increase transparency within the regulatory system. A higher degree of transparency would lead to banks performing above the required disclosure requirements and satisfying a great number of financial investors. We believe that the formation of different task, interest, and expert groups could contribute to increasing the awareness of the business and investment community regarding the importance of sustainability information. Its economic relevance should be communicated and understood from a spectral and interdisciplinary perspective. This knowledge transfer would be beneficial for several stakeholders, enhancing their understanding of how to unlock the opportunity embedded in spreading social and environmental value.

There are several clear implications for policy and practice based on the findings of the current study. First and foremost, key stakeholders in banking and capital markets (e.g., banking and finance associations, authorities, regulators, banks, academicians and shareholders, and wakf boards) must have increased awareness and understanding of the positive impact of the sustainability information narrated in both the IB annual reports and corporate websites. For instance, to enhance transparency, accountability, and credibility, regulators should consider introducing a mandatory, standardized framework on SRI reporting requirements. This would help in attracting a broader range of investors, who could in turn harness a better profitability in the long run. Not only should regulators increase pressure on firms to be transparent and accountable, they should also engage in the monitoring of potentially costs of Islamic banks adopting and implementing sustainable disclosures, in certain instances, particularly where litigations or ethical violations need to be investigated, reported upon, and acted upon. It is also important as such monitoring could also be of significant benefits to Islamic and ethical investment researchers as well where whistleblowing activities could improve awareness and strength and prospects of ethical repricing within firms.

**Future Research Directions**

The empirical understanding of more profit and loss sharing-based financial institutions than Islamic banks should be examined as individual cases, such as Baitul Mal Wat Tamwil (BMT), Lembaga Keuangan Mikro Syariah (LKMS) or others. This book adds the opportunity of a systematic nature to future research breakthrough for many academics from various areas of expertise.

Finally, the future research direction has demonstrated that there are many untouched areas where researchers can contribute to. This book has several limitations that can be rectified in future studies by other researchers with new ideas. For example, this book studies Islamic banks as representatives of financial institutions but other capital market instruments, such as sukuk, Islamic joint funds, takaful and other Islamic products, could be the topic of future studies.

There are many models, such as the maqasid al-sharia paradigm in examining Islamic financial issuance, cash waqf and prosocial behavior-based models to contribute to current literature in terms of economic and social development as well. There are various theories, such as the stakeholder theory, rich-get-richer and corresponding theories of the mission-driven business for explaining the services of Islamic banks. Various Islamic banking stakeholders are promoting the functions of Islamic financial institutions as intermediating, asset-creating and renewables-based banks. Many interesting questions, such as the outcomes of investment in the Sharia principle, the establishment of Universal Investment Account (UIA) and the purpose of two supervisory organizations, Bank Muamalat Indonesia and Shariah Insurance, should be explored. we have discussed the underlying principles of Islamic banks as representatives of financial institutions that operate under ethical considerations. Plenty of research has been conducted regarding the business models and performance of Islamic banks. However, the popularity of Islamic banks tends to increase with Islamic and non-Islamic societies, particularly after the 2007-2008 global financial crisis.

Islamic financial institutions consume arisen as essential objects within the kingdom of sustainable finance, as their foundational philosophies are basically allied with all-embracing objectives of long-term community and financial development. This study has established that Islamic financial tools, particularly those based on profit-sharing and ethical asset models, current a possible other to traditional banking systems in proceeding sustainability. Yet, notwithstanding the praiseworthy progress that Islamic banks have reached, here leftovers important possibility for improvement, chiefly concerning the intensification of their charities to social evenhandedness and ecological sustainability. Orderly policy improvements and further novelties within the Islamic finance domain are authoritative to understand its full possible. By supplementing their appointment in maintainable finance, Islamic banks own the volume to arise as foremost materials for global creativities aimed at development economic and social growth, chiefly in regions such as the MENA, where differences and developing tests are acutely marked.

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