

The Future of Islamic Finance in Central Asia



Acknowledgement

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This is a joint report of the Eurasian Development Bank (EDB), the Islamic Development Bank Institute (IsDBI), and the London Stock Exchange Group (LSEG), focused on a comprehensive analysis of the current status and future potential of Islamic finance in Central Asia. The report assesses both the quantitative and qualitative aspects of the Islamic finance market in Central Asia, including market size, growth trends, regulatory frameworks, success stories, and key challenges faced by financial institutions and stakeholders. It provides practical recommendations and strategic considerations tailored to the specific dynamics of the region, addressing regulatory harmonisation, capacity building, product innovation, and awareness campaigns.

Keywords: Islamic finance, Central Asia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan,

Uzbekistan, multilateral development banks.

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The team wishes to express its heartfelt gratitude to the President of the Islamic Development Bank, H.E. Dr. Muhammad Al Jasser, and the Chairman of the Management Board of Eurasian Development Bank, H.E. Mr. Nikolai Podguzov, for having confidence and trust in us to produce this report.

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We hope that this report will contribute to the development of the Islamic finance industry in Central Asia and will serve as a reference for all stakeholders in their endeavors to use Islamic finance as a means of socioeconomic and sustainable development in the region.

Sincerely,
Report Team

DISCLAIMER

The data of this report are believed to be correct at the time of publication but cannot be guaranteed. Please note that the findings, conclusions and recommendations that EDB, IsDBI and LSEG deliver will be based on information gathered in good faith from both primary and secondary sources, whose accuracy we are not always able to guarantee. The findings, interpretations, and conclusions expressed in this report do not necessarily reflect the views of EDB, IsDBI and LSEG. As such, the information contained in this report is intended to provide general information only and, as such, should not be considered as legal or professional advice or a substitute for advice covering any specific situation. EDB, IsDBI and LSEG disclaim all liability arising out of any reliance placed on this material. EDB, IsDBI and LSEG make no representations or warranties of any kind, express or implied about the completeness, accuracy, reliability or suitability of this material for your purposes.

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ABOUT US

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The Islamic Development Bank Institute (IsDBI) stands as a beacon of knowledge within the IsDB Group, pioneering innovative solutions to the economic challenges faced by Member Countries and Muslim communities through the lens of Islamic economics and finance.

Founded in 1981 as the Islamic Research and Training Institute (IRTI), the Institute underwent a transformative rebranding in 2021 to become the IsDB Institute. This evolution aligns our mission with the strategic priorities of the IsDB, enhancing our capacity to deliver tangible, sustainable value that elevates the wellbeing of our member countries and Muslim communities in nonmember countries.

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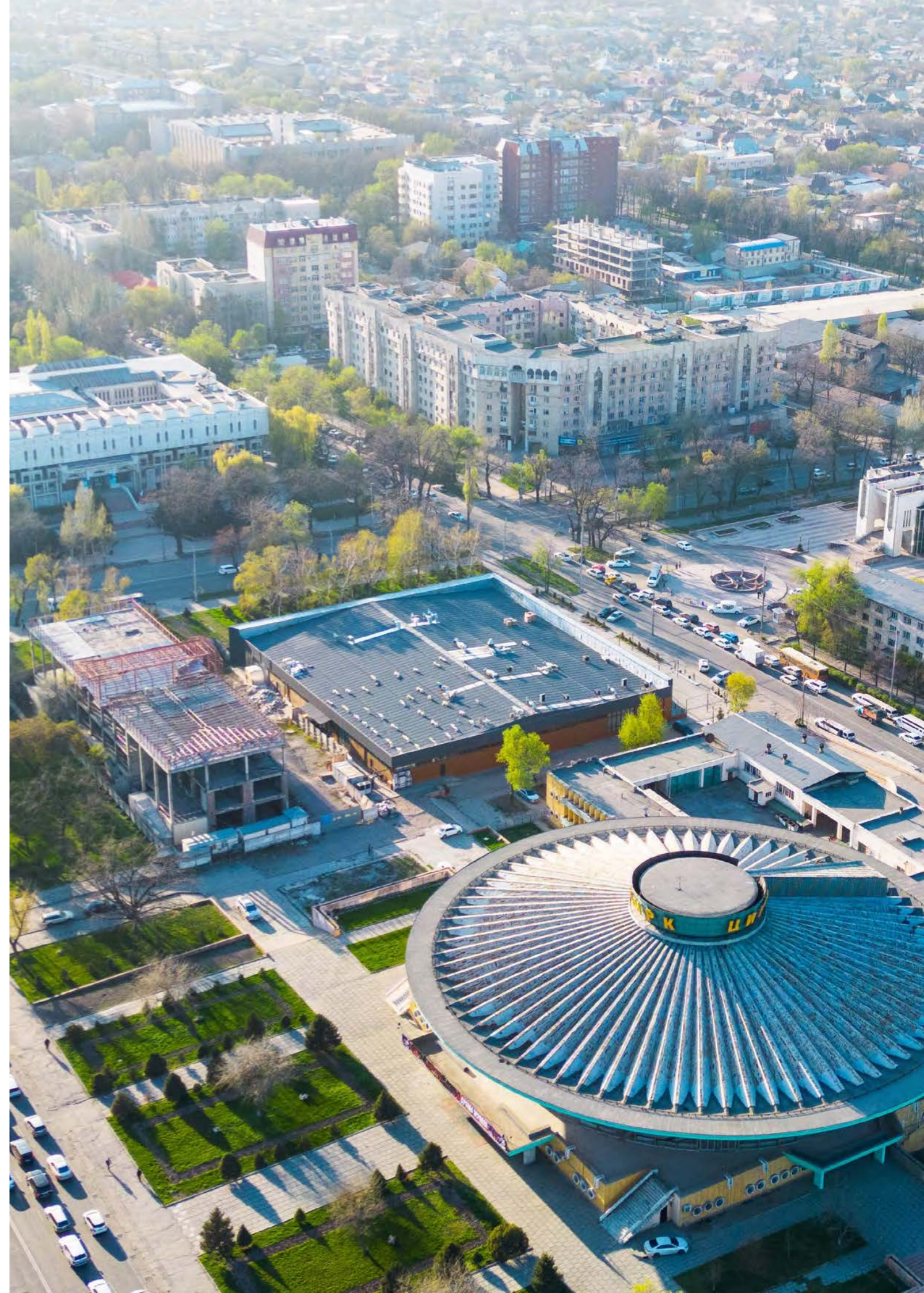
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Abbreviations

AIFC	Astana International Finance Center	IsDBI	Islamic Development Bank Institute
BCBS	Basel Committee for Banking Supervision	IsDB	Islamic Development Bank
CA	Central Asia	JSC	Joint-stock company
CAGR	Compound annual growth rate	KGS	Kyrgyz som
CAREC	Central Asia Regional Economic Cooperation	KZT	Kazakh tenge
CJSC	Closed joint-stock company	LC	Leasing companies
DFI	Development Finance institution	LSEG	London Stock Exchange Group
EDB	Eurasian Development Bank	Ltd	Limited liability company
ESG	Environmental, Social and Governance	MDB	Multilateral development bank
ETF	Exchange-traded fund	MENA	Middle East and North Africa region
FTSE	Financial Times Stock Exchange	MFI	Micro Finance Institutions
GCC	Gulf Cooperation Council	NBFIs	Non-Banking Financial Institutions
GDP	Gross domestic product	NBRK	National Bank of the Republic of Kazakhstan
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	OIC	Organisation of Islamic Cooperation
ICD	Islamic Corporation for the Development of Private Sector	P2P	Peer-to-peer
IFI	Islamic financial institutions	SME	Small and medium enterprises
IF	Islamic finance	STB	Second-tier banksw
IFDI	Islamic Finance Development Indicator	UAE	United Arab Emirates
IFRS	International Financial Reporting Standards Foundation	UK	United Kingdom
IFSB	Islamic Financial Services Board	UNDP	United Nations Development Programme
IMF	International Monetary Fund	UN	United Nations
IO	International Organization	USA	United States of America
IOSCO	International Organization of Securities Commissions	USD	United States dollar

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Introductory Note by the Eurasian Development Bank's Chairman of the Management Board

The further development of Islamic finance in Central Asia will expand financial inclusion and connect local businesses to the global Islamic market, contributing to regional economic growth.

The Eurasian Development Bank intends to become a platform for the development of Islamic finance in Central Asian countries. To this end, the Bank is currently working on creating relevant institutional and administrative solutions to develop the Islamic finance industry in its member states, particularly in Central Asia. The Eurasian Development Bank is considering attracting investments, including issuing *Şukūk*, to finance projects in Central Asia.

We highly appreciate our cooperation with the Islamic Development Bank, which provides us its methodological and advisory support in implementing the principles of Islamic finance in our Bank's operations.

The Eurasian Development Bank is also undertaking economic studies that are relevant to Central Asia. This is our first report dedicated to Islamic finance in Central Asia, which we are happy to produce in cooperation with the Islamic Development Bank Institute. On the pages of this joint report, one can find estimates on the possible size of the Islamic finance market for Central Asian countries in the long term, in line with ideas for sustainable growth in Islamic banking volumes and the role of multilateral development banks for stimulating this expanding sector.

We believe that this paves the way for a long and bright cooperation between our institutions and hope that it contributes to the economic prosperity across Central Asia, as the heart of Eurasia.

H.E. Nikolai Podguzov,

Chairman of the Management Board, The Eurasian Development Bank



“

The further development of Islamic finance in Central Asia will expand financial inclusion and connect local businesses to the global Islamic market, contributing to regional economic growth.

Message from the President of the Islamic Development Bank

I am pleased to present the joint report titled “The Future of Islamic Finance in Central Asia”, developed by the Islamic Development Bank Institute and Eurasian Development Bank.

Islamic finance has become an important tool for addressing economic and social challenges, contributing to sustainable development and inclusive financial systems globally.

The Central Asian countries, namely the Republic of Kazakhstan, the Kyrgyz Republic, the Republic of Tajikistan, the Republic of Turkmenistan, and the Republic of Uzbekistan, are at a crucial stage in developing their financial systems and economic growth. With strong cultural traditions and a growing demand for financial options, the region has great potential for the growth of Islamic finance. This growth could help financial systems expand and achieve broader socioeconomic objectives.

The Islamic Development Bank Group is committed to supporting the advancement of Islamic finance in Central Asia and beyond. Our collaboration with Eurasian Development Bank demonstrates how development banks can work together to create inclusive and resilient financial systems.

The report's practical recommendations provide an excellent roadmap for governments, financial institutions, and other stakeholders to collaborate and unlock this potential.

Looking ahead, I am confident that Islamic finance will continue to have a significant impact on fostering shared prosperity and contributing to sustainable development in Central Asia.

We are committed to strengthening our relationships and expanding the positive influence of Islamic finance across this important region.

H.E. Dr. Muhammad Al Jasser,

Chairman of the Islamic Development Bank Group



“

Islamic finance will continue to have a significant impact on fostering shared prosperity.

Glossary

Arabic Terms

Arabic transliteration	Arabic word	English meaning
Halāl	حَلَال	Permissible, lawful, allowed.
Fiqh	فِقْه	Refers to the whole corpus of Islamic jurisprudence. In contrast with conventional law, Fiqh covers all aspects of life, be it religious, political, social, commercial or economic. The whole corpus of Fiqh is based primarily on interpretations of the Qur'an and the Sunnah and secondarily on ijma (ijmā' – consensus) and ijtihad (ijtihad – Individual judgment). While the Qur'an and the Sunnah are immutable, Fiqhi pronouncements may change due to changing circumstances.
Ijārah	إِحْرَاقَة	Leasing. Sale of the usufruct of an asset. The lessor retains the ownership of the asset, together with all the rights and responsibilities that go with ownership. A lease agreement whereby a bank or financier buys an item for a customer and then leases it to him over a specific period, thus earning profits for the bank by charging rental. The duration of the lease and the fee are set in advance. During the period of the lease, the asset remains in the ownership of the lessor (the bank), but the lessee has the right to use it. After the expiry of the lease agreement, this right reverts back to the lessor. This is a classic Islamic financial product.
Muḍārabah	مُضَارَبَة	A partnership whereby one party (the capital owner) provides capital to an entrepreneur to undertake a business activity; profit is shared between them as agreed, but any financial loss is borne only by the capital owner as his loss is his unrewarded efforts put into the business activity.

Murābahah	مُرَابَحَة	Sale at a specified profit margin. The term, however, is now used to refer to a sale agreement whereby the seller purchases the goods desired by the buyer and sells them at an agreed marked-up price, the payment being settled within an agreed time frame, either in instalments or in a lump sum. The seller bears the risks associated with the goods in possession until they are delivered to the buyer.
Qur'ān	قُرْآن	The sacred book of Islam.
Ribā	رِب	Interest. An increase, addition, unjust return, or advantage obtained by the lender as a condition of a loan. Literally, increase or addition or growth. Technically, it refers to the "premium" that must be paid by the borrower to the lender along with the principal amount as a condition for the loan or an extension in its maturity.
Sharī'ah	شَرِيعَة	Islamic law. Refers to the corpus of Islamic law based on Divine guidance as given by the Qur'an and the sunnah, which embodies all aspects of the Islamic faith, including beliefs and practices.
Şukūk	صُكُوك	Islamic bond (Şukūk). Similar to an asset backed bond, Şukūk is a form of commercial paper that provides an investor with ownership in an underlying asset, and a return based on this ownership. Plural of 'Sakk', which refers to a financial paper showing entitlement of the holder to the amount of money shown on it. Technically, Şukūk are financial instruments entitling their holders to some financial claims.
Sunnah	سُنَّة	Tradition of the Prophet Mohammed.
Takāful	تَكَاوُل	Islamic insurance. Based on the principle of mutual assistance, Takāful provides mutual protection of assets and property and offers joint risk-sharing in the event of a loss by one of the participants. In case of loss to any one of the group, the loss is met from the collected funds.

Executive Summary

This report examines the potential of Islamic finance to foster sustainable economic growth in Central Asia. It evaluates the current state of the sector, highlights opportunities and challenges, and offers actionable recommendations to unlock its growth.

With reported total Islamic finance assets of USD 699 million in 2023, or 0.01% of total global assets, Central Asian nations still make a modest contribution to the industry. This is despite the large average share of the Muslim population, which constitutes 85% of the total population in these countries.

The region is served by full-fledged Islamic banks, Islamic banking windows, takaful operators, microfinancing, investment, leasing companies, and Islamic FinTechs. However, Islamic capital market instruments are developing more slowly than Islamic financial institutions.

The Islamic finance journey for each of the Central Asian countries began with joining the IsDB grouping of member states in the 1990s, with Kyrgyzstan being the first to join. Apart from the Republic of Turkmenistan, which does not currently have any Islamic financial institutions, most countries have made significant strides in their local industries since then. Each Central Asian country has different sectors contributing to their overall Islamic finance industries.

In terms of regulatory frameworks and legal environments, the region is relatively nascent compared to highly developed Islamic finance markets. Among the Central Asian countries, Kazakhstan and the Kyrgyz Republic have made significant progress in establishing their regulatory and legal frameworks for Islamic finance.

Despite the developments in the region, challenges exist. Key challenges facing the regional Islamic finance industry include limited awareness, a shortage of talent, and the need for harmonisation of regulatory frameworks. Additionally, regional opportunities exist that can bode well for the region's Islamic banking and finance industry.

Overall, Islamic finance offers a unique opportunity for Central Asia to promote inclusive growth, financial stability, and sustainability. Overcoming these challenges will require coordinated efforts and innovative solutions. By capitalising on its strategic advantages, the region can position itself as a key player in the global Islamic finance industry.

In conclusion, it is expected that the industry in the region will continue to grow, with projected sukūk assets of USD 5.6 billion and Islamic banking assets of USD 6.3 billion by 2033. Given the demographics as well as economic growth and size of the banking industry in each of the five Central Asian nations, Kazakhstan is likely to be the main driver of this growth, followed by Uzbekistan and Tajikistan.

This assumes that the governments in the region will actively work to create a facilitative environment for Islamic finance, putting in place appropriate regulatory regimes and other elements of the supporting ecosystem of the industry. These projections are also aligned with the experiences of other emerging Islamic finance markets.



1. Key Numbers

\$4.9t

Global Islamic Finance Assets in 2023

\$699m

Central Asian Islamic Finance Assets in 2023

\$2.5b

Central Asian Islamic banking assets in 2028(P)

18

Islamic Banks and Windows

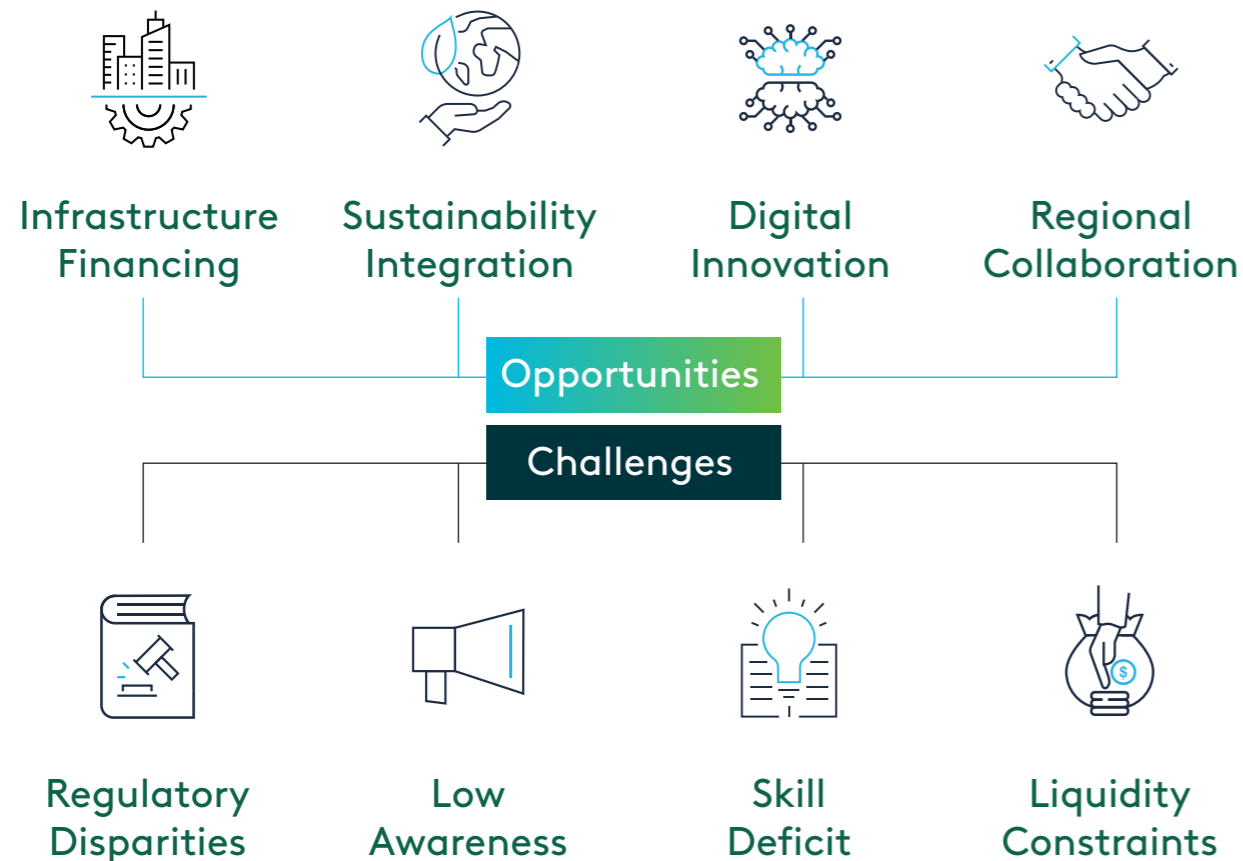
14

Islamic Non-Banking Financial Institutions

3

Countries with Islamic Finance Regulations

2. Opportunities & Challenges



3. Strategic Recommendations

1. Regulatory Alignment:

Create standardized frameworks aligned with global Islamic finance standards to attract international investments

2. Skill Development:

Launch training initiatives to address talent shortages and collaborate with global institutions to transfer expertise

3. Product Customization:

Design products tailored for sectors like microfinance, agriculture, and renewable energy to meet local demands

4. Awareness Programs:

Increase public and institutional understanding of Islamic finance through targeted campaigns and success stories

5. Technology Adoption:

Utilize FinTech to expand access to Sharī'ah-compliant financial services and drive innovation in the sector

4. Outlook for Central Asia

Şukūk Assets

\$2,053m

\$5,593m

2028

2033

Islamic Banking Assets

\$2,538m

\$6,295m



Chapter 1. Introduction

1.1 Background

Islamic finance or Shari'ah-compliant financing, as a relatively new (more than 30 years old) and fast-growing segment of the global financial system, plays an increasingly important role in the sustainable development of the Central Asian states (Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan).

The strategic role of Central Asia in the vast Eurasian space will be increasing: the region had an aggregate GDP of USD 453 billion in 2023 and will reach USD 675 billion in 2028 (IMF Data Mapper).

At the same time, the region has to overcome such challenges as the lack of access to the sea, resource dependence, a low level of financial and infrastructure development, the impact of climate change, and others. Islamic finance provides opportunities to attract significant resources for unlocking the region's potential, including the development of national financial markets, energy, transport and social infrastructure, labour markets, etc.

All Central Asian states governments are paying special attention to the development of Islamic finance. Some countries have enacted legislation to establish the relevant financial segments such as banking and leasing. The instruments of Islamic finance, discussed in detail in this report and focused, among other things, on achieving the UN's global Sustainable Development Goals and adaptation to climate change, are being implemented by an increasingly wide range of financial organisations, including national regulators, commercial banks, and multilateral development banks. These organisations are gradually forming a global network that also includes the Global Islamic Finance and Impact Investing Platform established by the IsDB and UNDP; regional Islamic finance hubs, like the IsDB Hub in Kazakhstan; Islamic finance windows, etc. At the same time, the institutional infrastructure of Islamic finance needs new development incentives, including educational programs, initiatives for producing and sharing of knowledge and best practices.

Due to the specificity of this segment of the global economy and some fragmentation of open data about it in Central Asia (CA), it seems useful to present the results of an independent study on the current state and trends in the development of national Islamic finance markets in CA countries.

This report consists of five chapters, with the first one containing an introduction and a literature review. The second chapter is devoted to the global trends and best practices of Islamic finance. The third chapter describes the current situation in Central Asian countries, including dynamics and key trends, the regulation environment, challenges and opportunities of the Islamic finance industry. The fourth chapter gives a quantitative assessment of CA national markets for Islamic finance, especially the estimated size of the Islamic finance market for each country. The last chapter includes a qualitative assessment of the Islamic finance trends in Central Asian countries over 5-10 years, prospects of Central Asian players in attracting external Islamic funding, and the role of national, foreign, and multilateral financial institutions in Islamic finance industry development, with recommendations to the governments and businesses of the region.

1.2 Literature Review

There is quite a significant pool of research in terms of the development of Islamic finance. However, the number of publications on the Central Asian region is insufficient, especially in terms of quantitative estimates of both current and prospective, but the growing interest to this perspective financial sector needs and stimulates research work worldwide. And one of the most fresh and deep overview, focused on the Central Asia+ region, is the report of the Research Center for Islamic Economics (IKAM), which analyzes the Islamic Finance landscape in Central Asian states and Russia (Nagaev et al., 2022). This report highlights industry's key challenges such as lack of public awareness and Islamic financial literacy, a shortage of qualified human capital, double taxation and government support, that actualises a need to develop a complete Islamic Finance infrastructure in the mentioned states including all segments such as Islamic banking, Islamic capital market, Islamic insurance (Takāful), Islamic social finance and Ḥalāl sector.

Also we should mention here some country papers and policy briefs, showing the perspectives and a need for the systemic institutionalization of Islamic finance and offering recommendations for policy development. For example, the Kazakhstan's Astana International Finance Center (AIFC) draws attention to the progress of Islamic finance industry in this country as a regional frontrunner that is shown by the survey conducted with technical assistance of the IsDBI (AIFC, 2024a, 2024c). In particular, the AIFC highlights its regulatory framework that permits designated entities to undertake a broad spectrum of finance activities, compliant with Shari'ah principles. At the same time, the AIFC underlines such current specifics of the industry, that the development of Islamic financial products for both retail and corporate segments primarily interests practicing / deeply religious Muslims, while Islamic financial principles may not be a critical concern for individuals of other religions or non-religious, that are interested mostly in economic benefits and financing conditions of banking products. In addition, it is important to mention that Kazakhstan was globally ranked as 19th in the Islamic Finance Development Indicator (IFDI) 2024 (ICD – LSEG, 2024).

Situation in Uzbekistan is shown by the Center for Progressive Reforms, underlining a need of substantial attention and comprehensive solutions from the state government, including the cooperation with the IsDB Group, to unpack all potential benefits and opportunities offered by Islamic finance (Fanger, 2023).

Many other research works and publications, reflected in the present paper, are focused on the regulatory landscape governing Islamic finance in each country, being analyzing existing laws, recent reforms, and the alignment of these laws with practices adopted among countries with mature Islamic finance. These documents, in line with the present joint IsDBI – EDB report, assess the potential for growth within Central Asian markets, providing case studies and insights on successful Islamic finance projects, institutions and best practices for the region.

Chapter 2. Islamic Finance – Global Trends



2.1 Global Islamic Finance Landscape

The Islamic finance industry has seen an accelerated growth into a global market since its emergence in the 1970s. The Islamic finance market was present in 90 countries in 2023, whether through Islamic financial institutions or Islamic capital markets. The industry is based upon the expanding economic presence of Muslim populations worldwide and their search for Shari'ah-compliant financial services. The industry is based on rejection of interest payments (ribā) and reliance on investments in real economic activities.

Sustained growth in Islamic finance assets continued during 2024, although slower than in previous years due to the global economic slowdown.

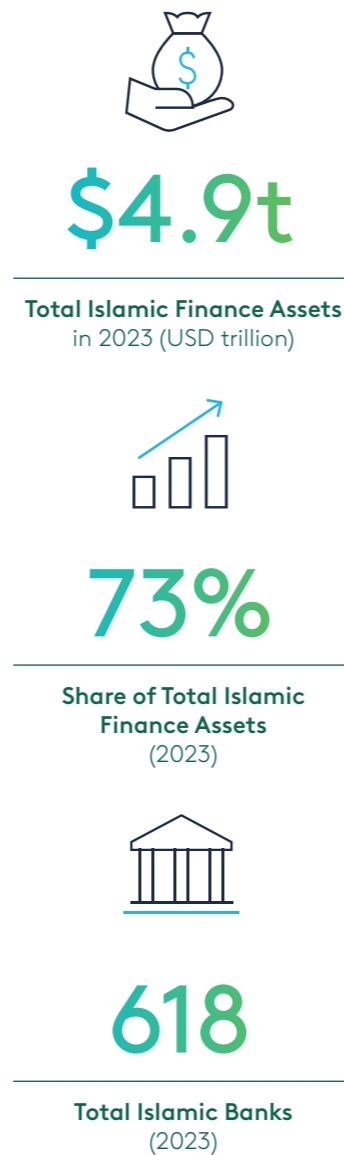
Total Islamic finance industry assets grew 11% to USD 4.9 trillion from 2022 to 2023, according to the ICD-LSEG Islamic Finance Development Report 2024. Among the fastest-growing countries during this period are the Central Asian nations of Kyrgyzstan and Tajikistan, whose performances will be detailed in the next chapter of this report. The Islamic finance industry grew by 175% since 2012.

Factors contributing to the industry's growth globally include the presence of at least one type of Islamic finance regulation in 57 countries, central Shari'ah boards operating in 23 countries, and more than 1,500 Shari'ah scholars representing Islamic financial institutions.

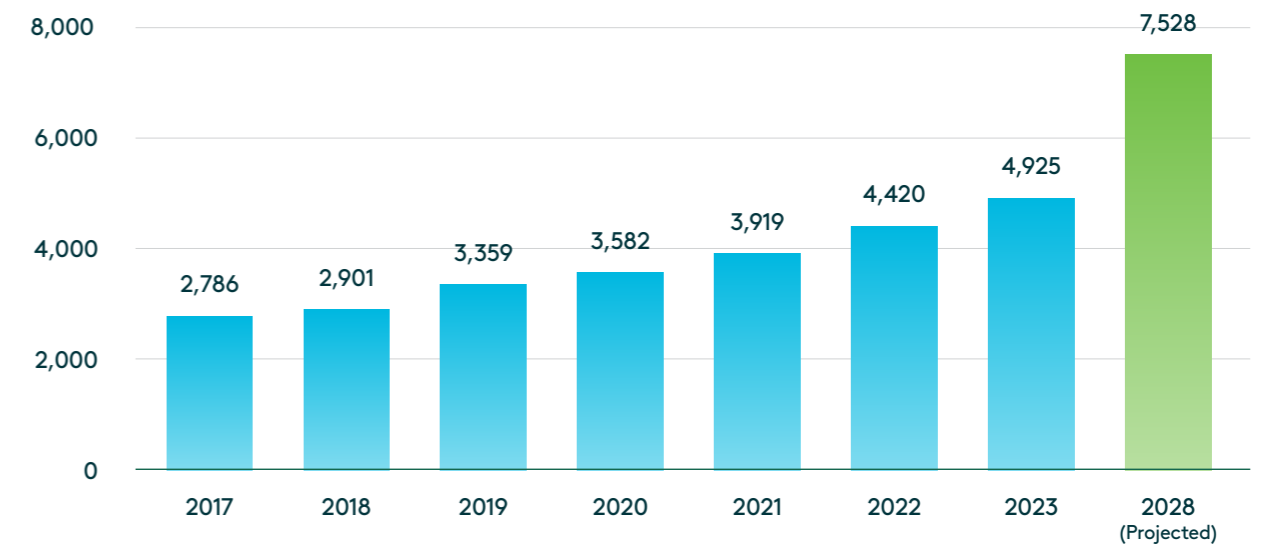
These statistics and the developments outlined are just some of the contributors towards the industry's development over the past years. According to the Islamic Finance Development Report, it is expected that the Islamic finance industry will continue its growth trajectory to reach USD 7.5 trillion in assets by 2028.

The Islamic finance market was present in 90 countries in 2023, whether through Islamic financial institutions or Islamic capital markets.

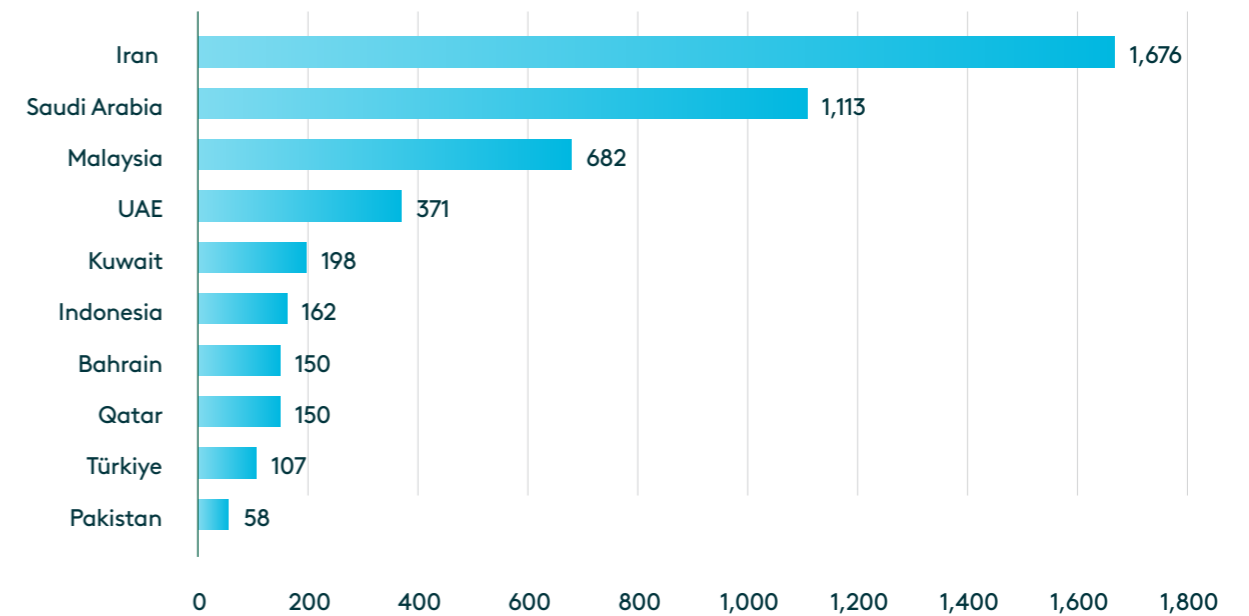
Figure 2.1.1: Global Islamic Finance Industry Landscape in 2023



Islamic Finance Assets (2017 - 2023, USD billion)



Top Countries in Islamic Finance Assets (2023, USD billion)



Source: IsDBI - LSEG analysis, authors' estimates

Sustained growth in Islamic finance assets continued during 2024, although slower than in previous years due to the global economic slowdown.

Islamic Financial Institutions

Islamic Banking

Largest Islamic finance sector and main driver of industry's growth

The Islamic banking sector accounts for the majority of Islamic finance assets, with a 73% share in 2023. This is due to the strong presence of Islamic banks and Islamic banking windows in the Middle East and North Africa (MENA), Southeast Asia, and South Asia. The sector grew 11% since 2022, due mainly to growth in the main Islamic finance markets.

The sector continues to see new countries taking steps to incorporate Islamic banking in their financial systems in response to rising demand. The latest is Uganda, whose parliament in June 2023 removed legal roadblocks to incorporating Islamic banks in its financial system, followed soon afterwards by the issuance of the country's first Islamic banking license.

In addition, the sector has seen a number of consolidation activities, whether between Islamic banks or conventional banks, and even between Islamic and conventional banks.

Takāful and Other Islamic Non-Banking Financial Institutions (NBFIS)

Islamic non-banking financial institutions are playing a supporting role in the industry

Takāful, which is the Shari'ah-compliant alternative to conventional insurance, and is based on a co-operative system of reimbursement if there is a claim; it is the smallest sector in the global Islamic finance industry, and it grew by 1% to USD 86 billion in total assets in 2023. The sector is facing increased competition from its conventional insurance counterpart. It is mostly concentrated in the Gulf Cooperation Council (GCC) countries, Iran, and Southeast Asia. As with Islamic banking, the sector has seen some consolidation activity over the past few years.

Islamic financial institutions that are neither Islamic banks nor takāful operators fall under the non-banking financial institutions (NBFIs) sector. These institutions can be Islamic financing companies, Islamic Fintechs, Ijārah (leasing) companies, and Mudarabas. Saudi Arabia is home to the largest number of NBFIs, as more companies set up operations or opened a branch in the Kingdom.



\$3.8t

Total Assets
(2023, USD trillion)

73%

Share of Total Islamic Finance Assets
(2023)

618

Total Islamic Banks
(2023)

Source: ICD – LSEG Islamic Finance Development Report 2024



TAKAFUL



OIFIS

\$86b \$153b

Total Assets
(2023, USD billion)

TAKAFUL

OIFIS

2% 3%

Share of Total Islamic Finance Assets
(2023)

TAKAFUL

OIFIS

364 999

Total Institutions
(2023)

Source: ICD – LSEG Islamic Finance Development Report 2024

Islamic Capital Markets

Şukūk

Issuance growing in new markets as pipeline builds

Şukūk, which is the Shari'ah-compliant alternative to bonds, is a certificate that represents ownership of a portfolio of assets; it is the second largest contributor to Islamic finance assets. The sector has continued to see issuances from key Islamic finance markets such as Malaysia and the GCC, from sovereign, corporate, and quasi-sovereign issuers. Some niche markets are also stepping up their Şukūk issuance, including the sub-Saharan African nations of Tanzania and Nigeria.

A growing segment of the Şukūk asset class is ESG Şukūk, where issuance totalled USD 13.4 billion in 2023. Growth is expected to continue in the coming years, as many governments are setting sustainability objectives that can be partly achieved through the use of Islamic finance. Oman, for instance, in early 2024 issued a sustainable finance framework that includes the issuance of "Green, Social and Sustainability bonds, loans or Şukūk".

There is a growing pipeline of future Şukūk issuance as sovereigns and corporates await more favourable conditions, such as a lower interest rate environment, which would lead to lower profit rates.

Islamic Funds

High demand despite volatility

The Islamic funds asset class is an important component of the Islamic capital market. It is also the most volatile, given that most Islamic funds are invested in equities that are highly sensitive to market conditions.

During 2023, some Islamic funds saw negative growth due to adverse sentiment in equities as a result of multiple rate hikes imposed in many jurisdictions around the world.

Despite this, the asset class also saw a few notable fund launches in non-OIC markets, such as Australia's first Islamic exchange-traded fund (ETF), as well as Islamic ETFs aligned with ESG principles, which leverage synergies between Islamic finance and ESG to attract non-Muslim investors. These new launches reflect growing demand for Islamic funds, particularly in the area of index-investing.



\$863b

Total Value Outstanding
(2023, USD billions)

+5,000

Total Number of Şukūk Outstanding
(2023)

Source: LSEG Workspace



\$254b

Total Value Outstanding
(2023, USD billions)

2,399

Total Number of Islamic Funds Outstanding
(2023)

Source: LSEG Workspace

2.2 Issues Facing the Islamic Finance Industry Globally

Despite the development of the industry and milestones reached over the past decade, the Islamic finance industry globally is still characterised by the following:

A. Considerably higher cost of transactions

A higher cost of transactions is indeed, one of the major unresolved issues in the Islamic finance industry. Some would say that this is due to the economics of scale that the industry has not yet attained. Others might contend that the problem arises because of lack of legal and regulatory harmonisation, which contributes to an uneven playing field leading to a higher cost of transactions in Islamic financial products. Notwithstanding such arguments, this requires a solid solution, particularly in the area of home financing, which is ubiquitous in many Muslim countries and also for Muslim communities living in non-Muslim countries.

B. Limited options of risk management instruments, mitigation techniques, and quantitative measurement models

Despite numerous efforts by the Islamic Financial Services Board (IFSB) in issuing guidelines pertaining to risk management, stress testing, and capital adequacy standards, more detailed technical guidance which features the techniques and methodologies of risk assessment, taking into account unique risks in Islamic financial institutions (IFIs), is still required. Furthermore, it is also commonly understood that whilst the definition of risks in IFIs is not substantially different from that in their conventional counterparts, a modification in the identification, measurement, and mitigation of risks may be required due to Shari'ah principles.

C. Restricted legal and regulatory framework

A daunting task for IF industry stakeholders is not only to establish regulatory harmonisation between different jurisdictions, but also to conform with the standards and guidance set out by international standard setting bodies such as BCBS, IOSCO and IFRS. Surely, the idea of 'one size fits all' is not viable, since different countries have different institutional and regulatory frameworks. Hence, there is a dire need to develop a proper legal environment and suitable regulatory framework to encourage sound risk management for IFIs. In addition, limited liquidity instruments for Islamic capital markets are another challenge.

D. Lack of Islamic monetary policies

At the macro level, the availability of Islamic monetary instruments is indispensable to support the macroeconomic objectives of the Islamic financial system. Another important element of such an instrument is liquidity management. Some countries have initiated the creation of such instruments, such as Indonesia and Malaysia. However, more efforts need to be undertaken to also allow inter-jurisdictional transactions and liquidity management between the countries implementing an interest-free financial system.

E. Financial inclusion gap

Financial inclusion is a concept that has gained importance since the early 2000s, which initially referred to the delivery of financial services to low-income segments of society at an affordable cost. However, two distinct features which characterize the concept of financial inclusion from an Islamic perspective are a) risk-sharing, and b) redistribution of wealth. Although there is a strong demand for Islamic microfinance services in OIC countries, it is not met by the supply. A study by Mohieldin et al. (2011) shows that although OIC countries have more microfinance deposits and accounts per thousand adults than non-OIC countries, the values of micro finance institutions (MFI) deposits and loans as a percentage of GDP are still much lower in OIC countries (0.61% and 0.79%) compared with developing countries (0.78% and 0.97%) and low income countries (0.92% and 1.19%). The gap of microfinance in the OIC countries is not only demonstrated by its limited scope, but also by the lack of regulation in OIC countries compared to other developing countries. In the MENA region for example, only Egypt, Morocco, Syria, Tunisia, and Yemen have specific legislation for microfinance institutions.

F. Lack of alignment between industry needs and education

The continuing growth and intensified competition among market players in the IF industry has certainly posed quantitative and qualitative human resource problems for the industry. It does not come as a surprise, therefore, that the IF industry needs more and better-qualified personnel.

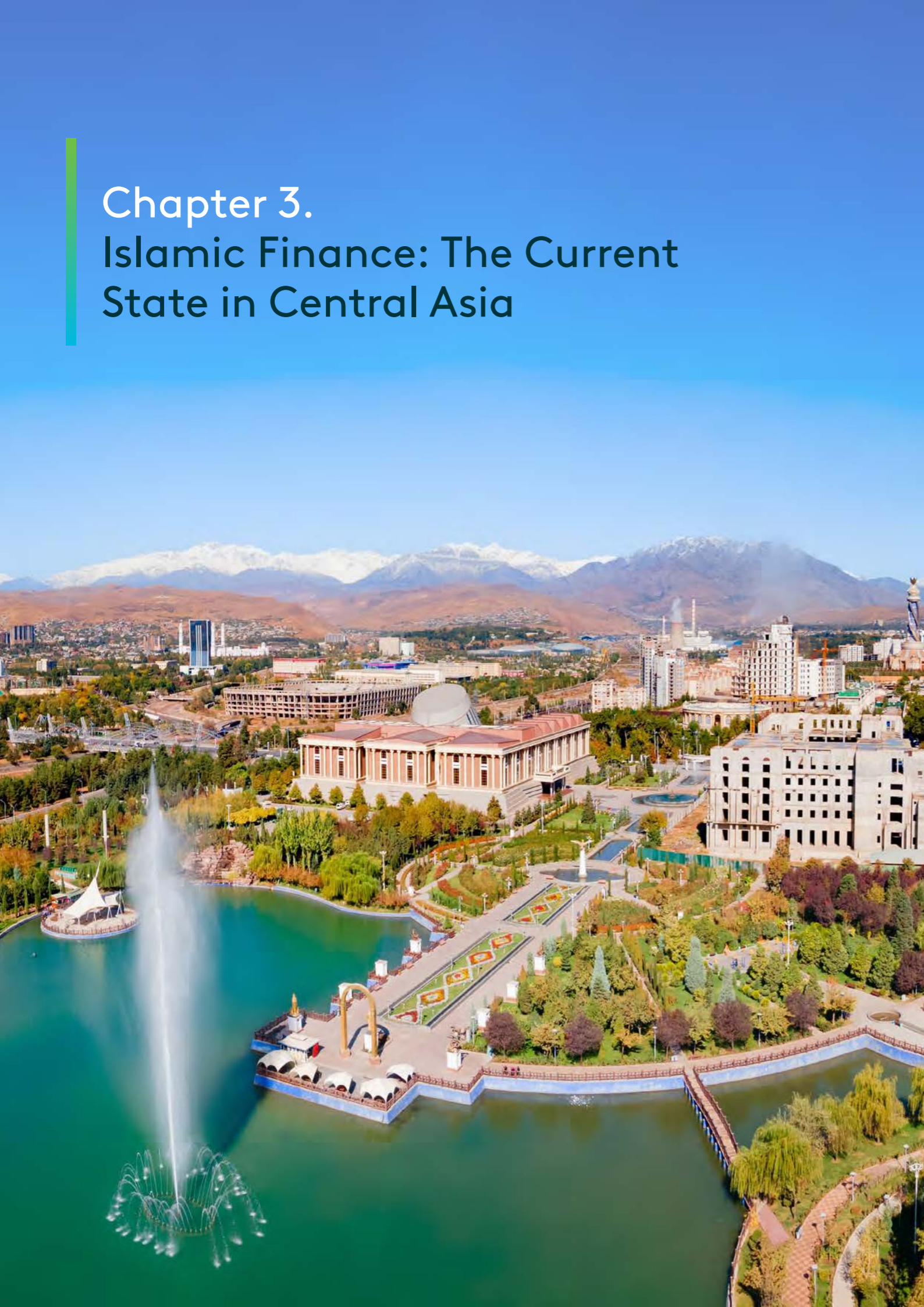
However, there is a ubiquitous inverse relationship between the growing number of Islamic finance education programs and the level of absorption of Islamic finance graduates in the job market. There are at least two possible explanations of this:

1. Although the IF industry has expanded around the globe quite a great deal, its institutional logic hasn't fundamentally changed; it is still essentially a debt-creating institution rather than an equity-based stimulating institution, which implies that the skillset and manpower required to manage such debt-creating institutions are not fundamentally different than the required skillsets to manage conventional counterparts. In other words, 'Islamic finance specialists' informed by Islamic economics and with a good grasp of Shari'ah-related contractual matters, governance, and fiqh-based financial engineering, are not necessarily relevant. As a matter of fact, most of the personnel of banks and capital markets are just obligated to execute what has been prescribed by the verdict of the respective Shari'ah boards.
2. Even though education provides knowledge of Islamic finance, the graduates are not necessarily getting the relevant practical skills and expertise needed in the market.

G. Perceptions about Islamic finance

Many still think that Islamic finance is basically an industry designed by Muslims and offered to Muslims only. Although this appears to be partially the case, nonetheless, the key spirit of Islamic finance is a lot more profound.

Chapter 3. Islamic Finance: The Current State in Central Asia



3.1 Current Landscape and Trends

A. Regional Overview

The Islamic finance industry first arrived in the Central Asia region in the 1990s, when the development of the industry and its ecosystems was initiated by countries of the region that first became member states of the Islamic Development Bank (IsDB). Central Asian countries still make only a modest contribution to the global Islamic finance industry, with reported Islamic finance assets of USD 699 million in 2023, or 0.01% of total global Islamic finance assets. According to the Islamic Finance Development Report 2024, Kazakhstan ranked 19 globally in the level of Islamic Finance development (i.e., above the global average) in 2024 and it leads the Central Asian market. The Kyrgyz Republic, Uzbekistan, and Tajikistan rank globally 32, 63, and 82, respectively, while Turkmenistan lags substantially behind, ranking 111. Despite this, the Islamic finance industry has considerable prospects for development in the region given that its Muslim population averages 85% of the total population in these countries.



Source: ICD – LSEG Islamic Finance Development Indicator 2024, authors' estimates

The Islamic finance industry in the region is mainly supported by full-fledged Islamic banks as well as Islamic banking windows. Other institutions include takāful operators, microfinancing, investment companies, Ijārah or leasing companies, and Islamic FinTechs such as digital banks and wealth management platforms. Islamic capital market instruments such as Şukūk are developing more slowly than Islamic financial institutions, however.

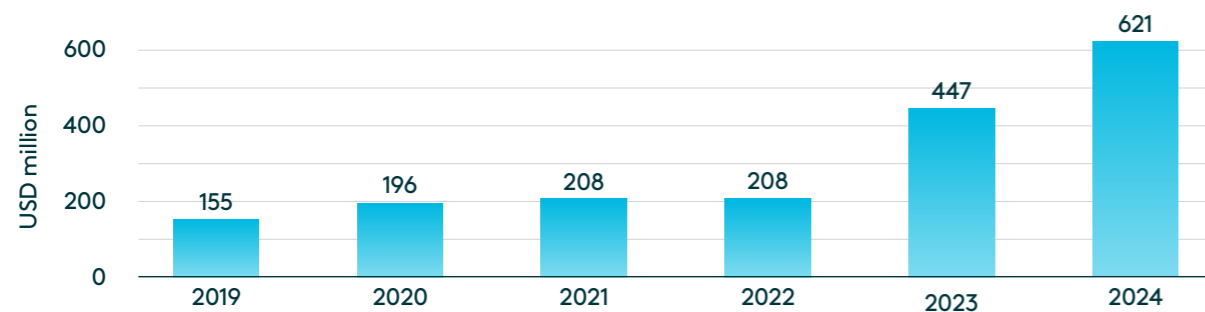
Figure 3.1.1:
Islamic Finance in Central
Asia in Numbers



B. Country Analysis

Kazakhstan: The country became an IsDB member state in 1995. Since then it has made numerous moves to develop its Islamic finance industry, including the establishment in 2010 of its first Islamic bank, Al Hilal Bank JSC, part of the UAE's Abu Dhabi Commercial Bank Group. The country's Islamic banking sector is the largest in the region, there now being two Islamic banks (Al Hilal Bank and Zaman Bank) with assets totalling USD 621 million as of January 1, 2025 (National Bank of Kazakhstan, 2024). The significant growth, almost tripling from USD 208 million in 2022, is mainly due to the new accounting treatment in Al Hilal Bank JSC's financial statements. This notable change is a result of amendments to the Resolution of the National Bank of the Republic of Kazakhstan (NBRK), which took effect in December 2023. These amendments require all Islamic banks to fully comply with the requirements of IAS 8 (IFRS, 2024) by recognizing all Islamic investment deposit liabilities and the corresponding assets funded by these deposits in their statements of financial position. These banks had to retrospectively restate the values for previous years.

Figure 3.1.2: Islamic Banking Assets in Kazakhstan



Source: Reported assets by Ecolslamic Bank, authors' estimates

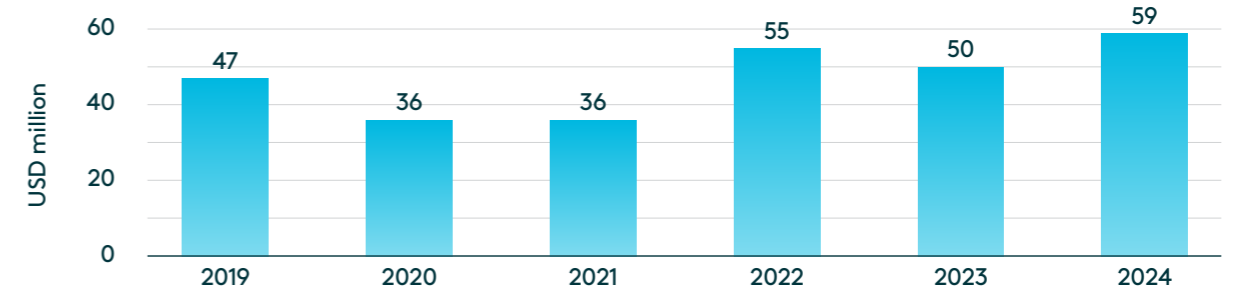
Kazakhstan also has one leasing (Ijārah) company, four Islamic banks, as well as an Islamic digital bank and investment firms. Islamic FinTechs have also tapped into the Kazakhstan market, among them the Ḥalāl investment app Wahed Invest, which has opened an office in Astana, the country's capital. At the same time, deposits in Islamic banks are not guaranteed in Kazakhstan (KDIF, 2022), especially because its national legislation does not allow the opening of Islamic finance windows – they should be either conventional banks or Islamic banks.

The Astana International Finance Center was established in 2015 to become a finance hub for the region, including Islamic finance. The first issuance of Ṣukūk was in 2012, when the Development Bank of Kazakhstan issued a USD 61 million Ṣukūk for listing on the Malaysian Stock Exchange (Reuters, 2018). The first-ever issuance of Kazakhstani tenge-denominated Ṣukūk followed in 2023, through which the Islamic Corporation for the Development of the Private Sector (ICD) raised KZT 2 billion (USD 4.45 million). These Ṣukūk were listed on the Kazakhstan Stock Exchange. Apart from this, Kazakhstan's financial trading platform Astana International Exchange has hosted cross-listings of Ṣukūk issued by Qatar International Islamic Bank and the IsDB.

The Astana International Finance Center was established in 2015 to become a finance hub for the region, including Islamic finance. Companies in the Islamic finance industry from the UK, USA, Malaysia, Bahrain, Qatar, Egypt, Kazakhstan and others are registered on the territory of the AIFC. In 2022, the "Alif Islamic Bank" received the license of AIFC as an Islamic bank.

Kyrgyz Republic: Kyrgyzstan in 1993 became the first Central Asian country to join the IsDB as a member state. In 2006, with the support of the IsDB, a pilot project was launched in the Kyrgyz Republic to introduce Islamic financing principles based on EcolslamicBank CJSC, which became the first bank in the Central Asian region to offer Islamic financing services (Kyrgyzstan Newline, 2023). According to the National Bank of the Kyrgyz Republic, operations based on Islamic financing principles are carried out by 14 financial and credit organizations of the Kyrgyz Republic: 1 pilot bank, 4 banks with an "Islamic window", 5 Islamic microcredit companies, 2 microcredit companies with an "Islamic window", 1 microcredit agency with an "Islamic window" and 1 Islamic credit union. The volume of financing based on Islamic principles in 2023 amounted to 6.1 billion soms (2.2% of the total volume of banks loans issued), after an increase of 1.3 times compared to 2019. Kyrgyzstan's reported Islamic banking assets amounted to USD 59 million in 2024.

Figure 3.1.3: Islamic Banking Assets in Kyrgyzstan

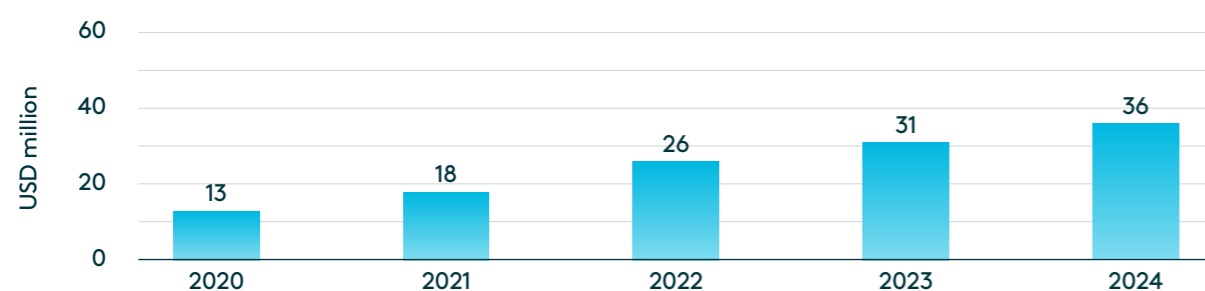


Source: Reported assets by Ecolslamic Bank, authors' estimates

There are state-owned enterprises providing Islamic finance services through their special windows: one Islamic leasing (Ijārah) company, one state mortgage company, and one guarantee fund. The country's first Ṣukūk issuance was a Mudaraba Ṣukūk issued by Intercascade Trade and Finance Ltd. in 2023 worth KGS 750 million (USD 8.4 million). The share of Islamic finance in the banking sector's loan portfolio was around 2% in 2022, while the share of Islamic finance in the loan portfolio of the country's microfinance institutions was 5.0%. The deposit portfolio of banks following Islamic financing principles is slightly more than 1% of the deposit portfolio of the banking sector.

Republic of Tajikistan: The country began its Islamic finance journey by joining the IsDB in 1996, but its first Islamic financial institution was only established in 2013: ASR Leasing. Its first Islamic bank, Tawhid Bank, converted from a conventional bank in 2019. Tajikistani FinTech Alif Bank also offers digital Islamic banking services. In general, according to the National Bank of Tajikistan, 1 Islamic bank and 2 “Islamic windows” of microcredit organizations provide services based on Islamic financing principles. There are also 5 branches and 33 banking service centers of Islamic credit organizations operating on the Islamic finance market of the country. The country’s Islamic banking sector had a total USD 36 million in assets in January 2025, which is 0.8% of the banking system’s assets (National Bank of Tajikistan, 2024), and a CAGR of 29.3% since 2020. The country also has one Ijārah company and two microfinancing companies with Islamic window operations.

Figure 3.1.4: Islamic Banking Assets in Tajikistan



Source: Reported assets by Ecolslamic Bank, authors’ estimates

Republic of Uzbekistan: Uzbekistan was the last Central Asian country to join the IsDB, in 2003, yet today it is actively developing its Islamic finance industry in order to serve its Muslim population, with many businesses and individuals declining to take on conventional loans due to their religious beliefs. Taiba Leasing in 2011 became the first Ijārah and Islamic financing company to operate in Uzbekistan, with a focus on machinery and equipment leasing. Another company with the same profile (including also murabaha services) is Uzbek Leasing International. One Islamic FinTech company and several commercial and wholesale conventional banks in Uzbekistan are planning to open Islamic window operations. Finally, there is one takāful operator, Apex Insurance. It should be added that Trustbank’s subsidiary Trast Muamalat provides Islamic leasing services and 12 banks provide murabaha services (a kind of trade contract with an agreed clear cost and markup of an asset) through credit lines from the Islamic Corporation for Development of Private Sector (Kun.uz, 2024; Fakhridinkhujjev, 2023).

Republic of Turkmenistan: Although Turkmenistan joined IsDB in 1994, the Islamic finance industry there is still in the early stages of development, with no Islamic financial institutions present to date nor a regulatory framework to support the industry. However, some steps have been taken, such as decision of Turkmenistan to take part in increasing the total capital of the IsDB (Turkmenportal, 2022), access for assistance of the IsDB Regional Hub in Almaty, that conducts relevant regular consulting and expert events in Turkmenistan (IsDB, 2023).

3.2 Legal, Regulatory, and Policy Environment

A. Regional Overview

The overall legal, regulatory, and policy environment in Central Asia is relatively nascent, especially when compared with highly developed Islamic finance jurisdictions such as the UAE and Malaysia. Among the Central Asian countries, Kazakhstan and the Kyrgyz Republic have made significant progress in establishing a regulatory and legal framework for Islamic finance.

Kazakhstan developed and implemented a multifaceted legal, regulatory, and policy environment that is conducive to Islamic banking and finance at a national level. The country has implemented legislation specific to domestic Islamic banking and finance activities and has drawn up regulatory guidelines for Islamic banks and Islamic financial institutions. Since its launch in 2018, the AIFC has developed policies and incentives that have been conducive to the growth of Islamic finance on a national scale, so much so that financial regulators in Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan have adopted a joint declaration on the possibility of using the AIFC as a springboard for joint development of the Islamic financial system regionally (IFN, 2022).

The **Kyrgyz Republic** has shown a similarly progressive approach to developing its legal framework for Islamic finance. In the first stage of the implementation of Islamic banking, basic legal acts were created. In the second stage, changes were made to the regulatory framework in order to create equal conditions for traditional and Islamic banking; amendments were made to banking, civil, and tax legislation; and the principles of cooperation with international organisations for the development of Islamic financing principles were clarified.

The other countries of the Central Asia region have made little progress in developing legal frameworks to support domestic Islamic banking and financing activities. Although **Tajikistan** introduced Islamic banking regulations in 2014 which were supposed to create a favourable environment for Islamic banking, there have been no further legal and regulatory developments for Islamic finance for a long time (Ministry of Justice Republic of Tajikistan, 2014). Only in 2022 the tax code was amended to eliminate double taxation on Islamic finance banks. As for **Turkmenistan**, it is difficult to comment definitively on its Islamic banking and finance landscape due to a lack of clarity about its Islamic banking and finance laws, regulations, and policies. To the best of our understanding, although Turkmenistan does not yet have Islamic banking and finance laws, regulations, or policies in place, it continues to participate in the process of analysis and discussion on such regulations and opportunities, including with international organisations of the IsDB Group (ITFC, 2022). As of 2023, **Uzbekistan** also has yet to implement Islamic finance-specific legislation (Centil.Law, 2023).

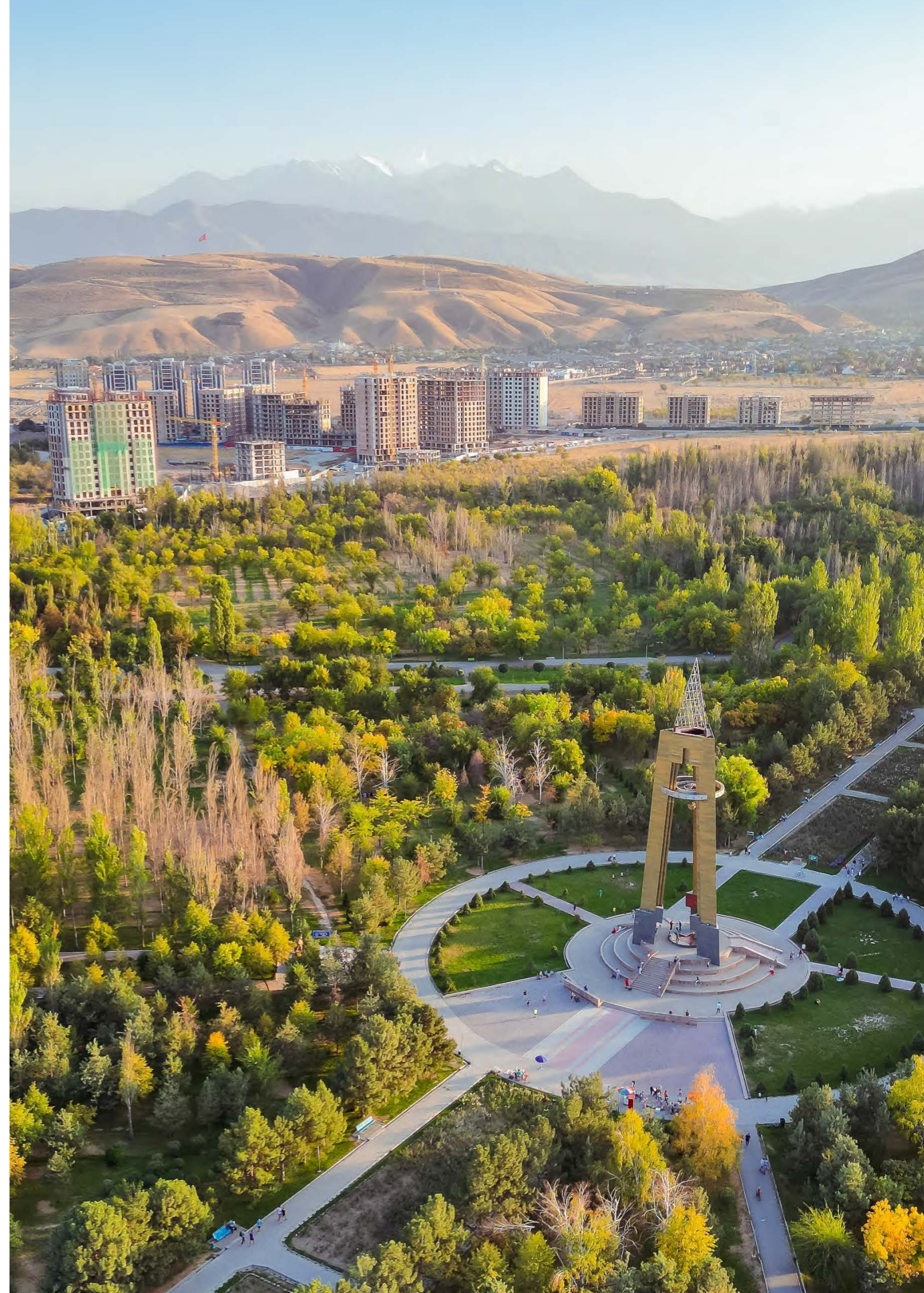
B. Country Analysis

Kazakhstan has been active in developing its legal and regulatory framework for Islamic banking. Although Islamic banking assets in Kazakhstan accounted for just 0.4% of all banking assets domestically as of January 1, 2024, the foundational legal and regulatory frameworks are already in place to facilitate further market growth (National Bank of Kazakhstan, 2024). Since 2009, the government has introduced various laws to enable the development of domestic Islamic banking, *Shūkūk*, and other Islamic finance. Moreover, the AIFC developed with the help of the IsDB and the Malaysian advisory firm ZICO Shari'ah the Islamic Finance Master Plan for the Republic of Kazakhstan 2020-2025, which includes a wide-ranging set of recommendations to guide domestic efforts to further boost Kazakhstan's ecosystem for Islamic banking and finance (AIFC, 2020).

Kyrgyzstan has also shown a progressive approach to developing an Islamic finance ecosystem, having introduced an Islamic banking to the Law "On Banks and Banking in the Kyrgyz Republic" and regulations on *takāful* in 2009. The Kyrgyz Republic is the first jurisdiction in Central Asia to amend its Civil Code, Tax and Customs Code to consider Islamic financial transactions (UNDP, 2023). Islamic finance principles have been incorporated in the amendments to the regulations of microfinance organisations. The concept for the development of an Islamic economic platform in the Kyrgyz Republic for 2023-2027 include the development of the Islamic insurance market (i.e., the possibility of organizing and launching a separate deposit insurance fund for financial and credit institutions operating according to Islamic principles) and the Islamic securities market, as well as increasing public awareness of Islamic finance. The goal is to achieve a share of financing according to Islamic principles of up to 5% of the loan portfolio of the financial system until 2025.

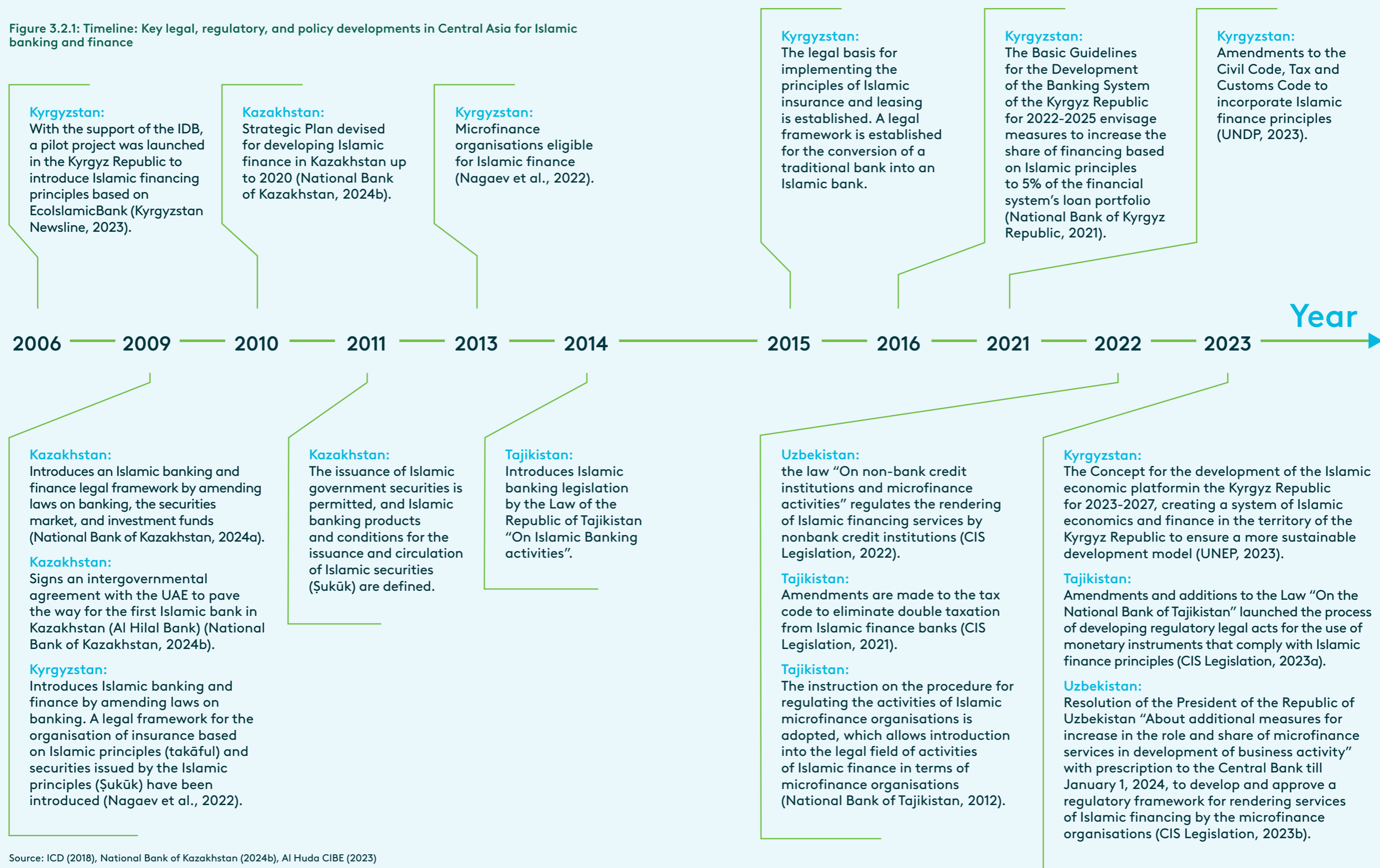
As mentioned, **Tajikistan** introduced an Islamic banking law in 2014. In 2022 the tax code was amended to accommodate Islamic finance principles. **Turkmenistan** does not appear to have introduced any regulations for Islamic banking and finance.

As of 2023, **Uzbekistan** is facing several obstacles to developing an Islamic banking and finance legal framework. The main blocks are a lack of Islamic banking and finance-specific laws; the continued adaptation of existing statutes and regulatory acts to the needs of conventional financial institutions without accommodating the needs of Islamic financial institutions; and the lack of a clear status for Islamic finance concepts and structures on the legal front. For example, common concepts in Islamic finance such as investment deposits, partnership-based arrangements, and purification of profits are not covered by any legislation or regulatory guidelines (Centil.Law, 2023; Nagaev et al., 2022). At the same time, the strategy "Uzbekistan-2030" sets the task of introducing criteria and procedures for Islamic financing in at least three commercial banks and the formation of a legislative framework for Islamic financing (The Government portal of the Republic of Uzbekistan, 2024). According to the Central Bank of Uzbekistan, the draft law has been submitted to the Cabinet of Ministers in 2024 and after finalisation will be submitted to the Parliament (Kun.uz, 2024). Finally, the law "On Non-Bank Credit Organisations and Microfinance Activities" has been amended to allow the provision of Islamic finance services in Uzbekistan (Lex.Uz, 2022).



Legal, Regulatory, and Policy Developments

Figure 3.2.1: Timeline: Key legal, regulatory, and policy developments in Central Asia for Islamic banking and finance



Source: ICD (2018), National Bank of Kazakhstan (2024b), Al Huda CIBE (2023)

3.3 Key Challenges, Opportunities, and Success Stories

A. Regional Challenges

There are at least three significant challenges facing the growth and development of Islamic finance in Central Asia (IFN, 2023). First, there is **limited public awareness** and understanding of Islamic financial principles. This hinders understanding of the products and services available and Islamic finance's value proposition. Second, qualified **talent** with professional expertise in Islamic finance remains scarce in the region, although that talent pool is expected to grow in the coming years. And third, there is a pressing need for **harmonisation of regulatory frameworks** at the regional level, which will first require adequate legal frameworks at the national level. Getting the relevant stakeholders together to solve these issues will be critical to Central Asia's success in unlocking its next stage of Islamic finance growth and development.

Because of these fundamental challenges, the Central Asian countries face another issue that is symptomatic of the nascent stage of their Islamic finance journeys: **low market share**. For example, as of January 1, 2024, Islamic banking assets made up just 0.4% of all banking assets in Kazakhstan (**National Bank of Kazakhstan, 2024**) and at end-2022, Islamic assets made up about 2% of all banking assets in Kyrgyzstan and 1.1% in Tajikistan (IFN, 2023). This was despite enabling regulations in Kazakhstan and Kyrgyzstan, and a pilot Islamic bank (Ecolslamic Bank) and three Islamic windows of conventional banks (Bakai Bank, JSC Kyrgyzstan, and OJSC Aiyl Bank) (IFN, 2022).

Other regional challenges include a general **lack of empirical research** on Islamic finance in the Central Asian countries (IFN, 2022), which could better inform stakeholders of gaps in the market and improve consumer perceptions and uptake of Islamic financial products and services.

B. Regional Opportunities

Despite these challenges, there are several opportunities that bode well for the growth of Central Asia's Islamic banking and finance industries (IFN, 2023). First, there is a clear opportunity to grow the Islamic banking and finance **market share** within the region given the current low baselines. For example, creating enabling legal and regulatory frameworks and providing specific incentives for Islamic finance transactions could boost participation by both local and foreign-based market participants, leading to an increase in market activities.

Second, **technology and digitalisation** could help Central Asian countries increase their market share. For example, building user-centric apps such as mobile banking, online platforms, and digital solutions could boost customers' access to Islamic finance products and services and improve customer experience. Moreover, Islamic banks can streamline their operations while building a wider customer base, especially among digitally native youth segments.

Third, there are opportunities to enhance Islamic finance in Central Asia via **partnerships** with institutions from more mature Islamic finance jurisdictions. These institutions and stakeholders can transfer expertise, knowledge, and resources to foster the Islamic banking and finance ecosystems in Central Asia. This partnership could be established with regional multilateral development institutions, like the Eurasian Development Bank, which could serve as a conductor for knowledge dissemination and a regional partner for Islamic investors as well.

Fourth, cultivating a steady pipeline of **regional talent** in Islamic finance could help the progress of the industry regionally. Some examples of relevant initiatives include workshops, educational certifications, and other forms of upskilling in Islamic finance.

Finally, although there is currently a strong focus on Islamic banking, it is helpful to take a more holistic view of the Islamic finance ecosystem and consider other aspects, such as development of the Islamic deposit guarantee system, Islamic microfinance, and Islamic FinTech ecosystems. More specifically, focusing on wider access to Islamic banking and finance services for rural areas, remote regions, and underserved communities, as well as providing more Shari'ah-compliant solutions and funding for SMEs, can invigorate not just Islamic finance in Central Asia, but the Central Asian economies as a whole.

C. Success Stories

In this section, we highlight some success stories in Islamic banking and finance in Central Asia under two key themes: infrastructure development, and Islamic digital banking and FinTech.

There are opportunities to enhance Islamic finance in Central Asia via partnerships with institutions from more mature Islamic finance jurisdictions.

Context

Islamic infrastructure development

In 2023, according to the OIC Infrastructure Outlook for that year (ICD-Refinitiv, 2023), Europe and Central Asia accounted for the third-largest regional gap in infrastructure funding, with an overall projected funding gap of USD 547 billion between 2016–2040. Türkiye made up USD 405 billion of this gap, while the rest of Europe and Central Asia were USD 142 billion short, including a gap of USD 84 billion for Kazakhstan alone. Roads made up 75% of the funding gap for Europe and Central Asia, indicating that regional road development remains a top priority for stakeholders. Given the landlocked nature of all five Central Asian countries, including the double-landlocked status of Uzbekistan, successfully improving the road and highway infrastructure in these countries can help unlock economic development, as this would enable better access to neighbouring countries' ports.

Two projects financed by the Islamic Development Bank (IsDB) serve to illustrate these benefits:

In **Tajikistan**, the IsDB in partnership with the Arab Coordination Group (ACG) reconstructed the Kulyab-Kalaikhumb road, which was especially challenging given the mountainous nature of the area. The resulting corridor, built in six phases between 2000 and 2020, remains the sole connector between Tajikistan's western and eastern regions, and extends as far as China. The key benefits of this use of Islamic finance include facilitating better travel and trade, opening up markets, and economically revitalizing the country (IsDB, 2024a).

In **Kazakhstan**, the IsDB reconstructed a core section of the Central Asia Regional Economic Cooperation transport corridor, a stretch of 58.1 kilometres that had fallen into disrepair. Kazakhstan's economic significance to Central Asia, and its wider potential to act as a strategic trade conduit between Asia and Europe, made the CAREC corridor's ability to connect Kazakhstan with China, Russia, and the other Central Asian countries pivotal to regional trade and economic links. However, the poor condition of the road had been causing rising numbers of traffic accidents, lengthy travel times, and missed business opportunities. To remedy this, the IsDB in cooperation with the Government of Kazakhstan sought to rebuild the transport artery of the country's Jambyl Region.

The project was completed within budget and six months ahead of schedule. It led to significant economic and social benefits for Kazakhstan, with an increase in daily traffic volume from 4,000 to around 6,000 vehicles, a halving of travel time between key cities, and a halving of freight transport costs. As a result, local businesses became more competitive and avenues to new agricultural zones and essential services were opened up (IsDB, 2024b).

Europe and Central Asia accounted for the third-largest regional gap in infrastructure funding, with an overall projected funding gap of USD 547 billion.

Islamic digital banking and fintech

Another success story in Kazakhstan is a program for lending to MSMEs on the principles of Islamic finance, that was launched in 2020 as a partnership of Damu Entrepreneurship Development Fund, Islamic Bank Al Hilal, and Kazakhstan Ijārah Company. Within the program, long-term financial support was provided to entrepreneurs using Islamic financial instruments.

The program is a pilot in Kazakhstan and will give an impetus to development of Islamic finance in Kazakhstan, giving entrepreneurs the opportunity to obtain alternative financing for business development. The program is implemented through purchase of goods on the commodity exchange for the purpose of financing STB/LC using Islamic finance instruments. A total of 12.25 billion tenge were placed in Islamic Bank Al Hilal JSC and Kazakhstan Ijārah Company JSC during 2020. According to the results of the year, 31 SMEs were financed under the program to the total amount of 11.4 billion tenge (DAMU, 2020).

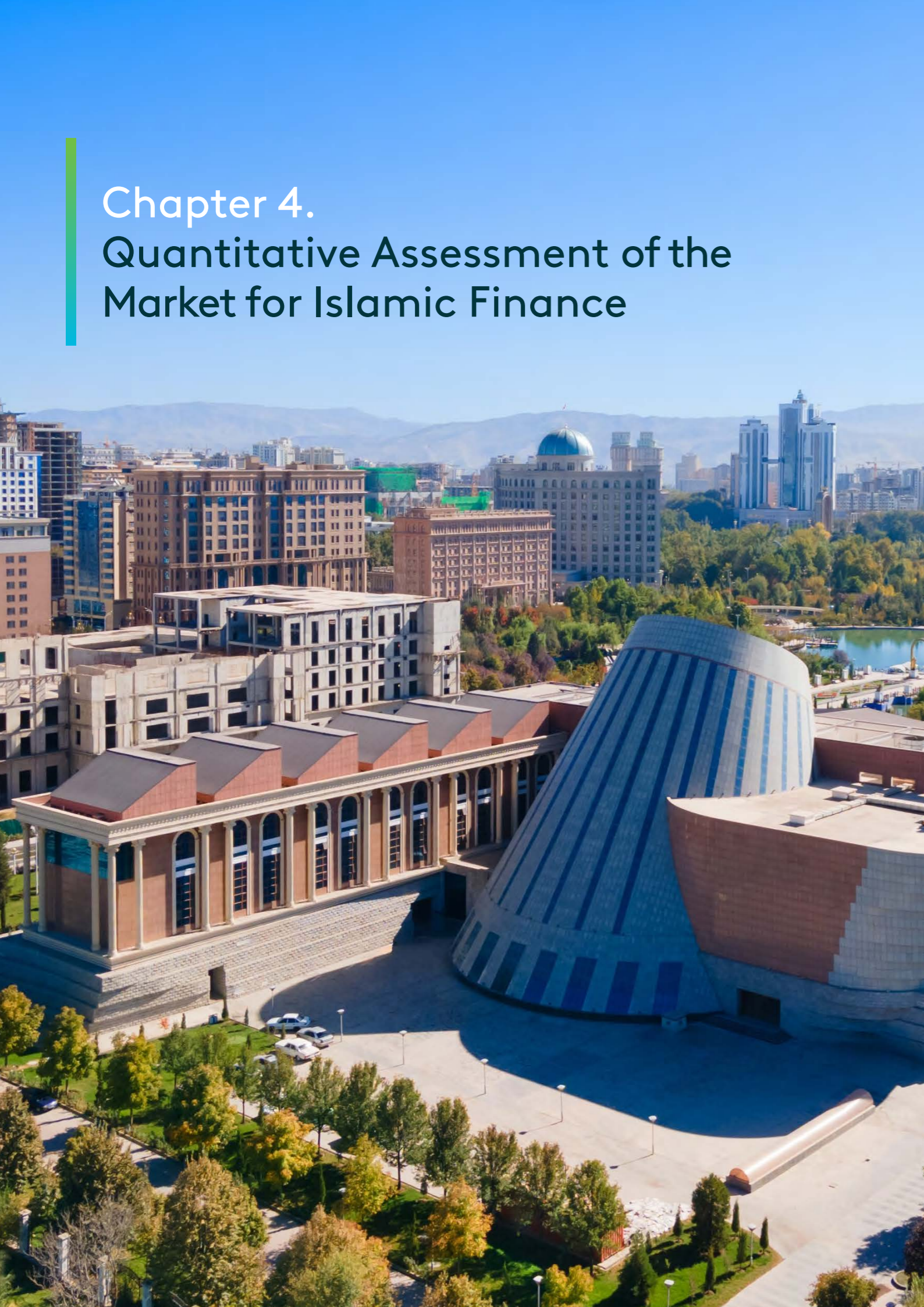
Broadly speaking, Islamic FinTech companies can potentially play a considerable role in the wider development of Islamic finance in Central Asia in at least two key ways. First, more success stories like Alif Bank and IMAN will likely encourage the rise of other success stories that build out the Islamic FinTech ecosystem across other yet untapped segments in Central Asian Islamic FinTech – e.g., Shari'ah-compliant blockchain and cryptocurrency use, crowdfunding and P2P finance, and takāful-based solutions (TakaTech). Second, increasing the number of Islamic FinTech companies and the coverage of Islamic FinTech sub-segments can probably help improve Islamic financial intermediation, especially among the youth demographic, who are digital-savvy and broadly interested in Islamic finance solutions. Currently, Islamic FinTech in Central Asia is still nascent, but with good growth prospects. For example, Kazakhstan's market size for Islamic FinTech, based on transaction volumes, is forecast to double from an estimated USD 15 million in 2022/23 to a projected USD 32.1 million by 2027, at a CAGR of 16.5% over the period 2022/23–2027. Similarly, Kyrgyzstan's Islamic FinTech market size is forecast to grow with a CAGR of 14.8% between 2022/23–2027 from an estimated USD 51.2 million in 2022/23 to a projected USD 102 million by 2027 (DinarStandard and Elipses, 2024).

Although Central Asia's Islamic FinTech ecosystem is still at a very early stage of development, there have been some success stories, including the two detailed below:

- **Alif Bank** is a Tajikistan-based digital bank that offers Alif Mobi, a payment app that allows users to make purchases, manage various instalments, and transfer money both domestically and internationally (Alif Bank). Alif closed a Series A funding round in 2021 with a valuation of USD 100 million during which it raised USD 50 million in debt and USD 8 million in equity. Alif Mobi has more than 483,000 active users in Tajikistan and has had more than 1 million downloads. Given this funding and traction, Alif looks well placed to make further inroads as a Shari'ah-compliant digital bank both nationally and regionally.
- **IMAN** is an Uzbekistan-based Islamic FinTech that runs both Iman Invest and Iman Pay. IMAN Invest is a wealth management platform for retail investors that uses a mudaraba-based structure to generate investment returns via the financing of trade deals in instalments (IMAN Invest), while IMAN Pay works with merchants to offer Shari'ah-compliant buy-now-pay-later (BNPL) services (500 Global, 2023). IMAN is backed by 500 Global, a prominent global accelerator, and presently operates in Uzbekistan and Kazakhstan, with plans to eventually expand into Pakistan, the broader South Asia region, and MENA (500 Global, 2023). In 2022, IMAN raised USD 1 million in a seed round from UAE-based investors (WAMDA, 2023).

Chapter 4.

Quantitative Assessment of the Market for Islamic Finance



4.1 Central Asia Region

The projected figures in this chapter are based on the assumption that the governments of these markets will actively work to create a facilitative environment for Islamic finance, putting in place appropriate legislative, regulatory and taxation regimes. They will also work to promote awareness and access to Islamic finance among the retail, corporate, and investment communities. Based on these assumptions, the projections are aligned with similar experience of other emerging Islamic finance markets.

Central Asia hosted a population of 79.3 million as of end of 2023 (IMF, 2024). The average Muslim share of the region’s populations is 85% (World Bank, 2024). Kazakhstan and Turkmenistan are considered upper-middle-income countries, while the other countries in the region are classified as low-income.

The average share of the adult population with accounts at financial institutions is 50%, according to the World Bank’s Global Findex Database for 2021, which collected information from Kazakhstan, Kyrgyzstan, Tajikistan, and Uzbekistan, as well as the 2017 edition of the Findex database, covering Turkmenistan (World Bank, 2022). While Kazakhstan has the highest such share at 81%, the rest ranged between 39% and 44%. An average 9% of those outside Turkmenistan cite religious reasons for not having an account. With regard to savings, 34% on average said they saved some money and just 7% saved at a financial institution.

Table 4.1.1: Central Asia Demographics

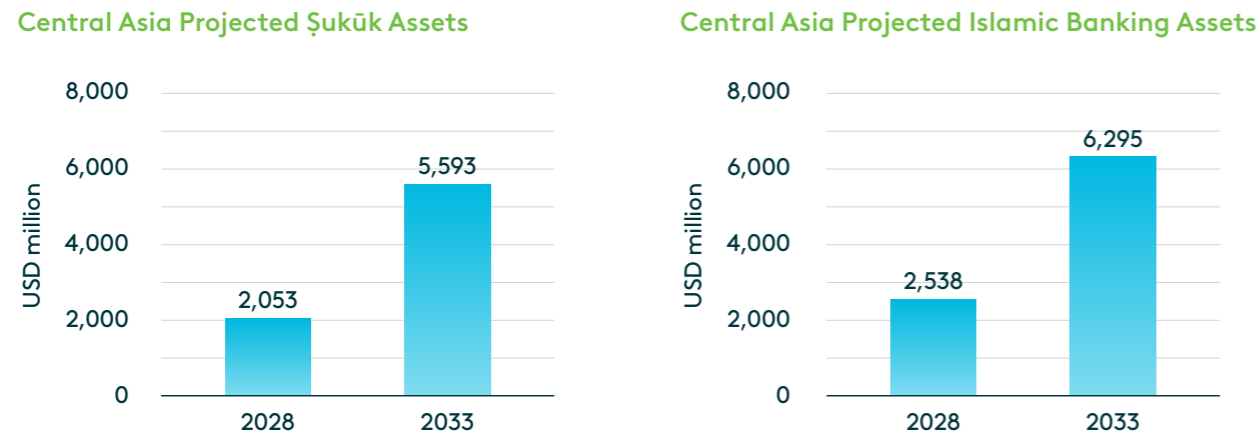
	Kazakhstan	Kyrgyzstan	Tajikistan	Turkmenistan	Uzbekistan
Population (2022), million	19.8	7.0	10.1	6.4	36.0
15 – 64 age (%)	62	58	58*	-	63**
Under 25 (%)	42	48,3	36***	-	45
Muslim (%)	70	90	97	93	88
No bank account (%), 2021	19	41	39.5	41	44
No account due to religion (%), 2021	5	8	9	-	16
Saved money (%)	40	32	18	51	28
Saved at institution (%), 2021	19	7	2	5	3

Note: *working age population, **16-64 age, ***younger than working age
Source: IMF, World Population Review, national statistical agencies, World Bank, authors’ estimates

There is much potential for the Islamic finance industry to develop across the Central Asia region, not just to meet the needs of the large underserved Muslim population, but also given that the Islamic finance stimulates to develop ḥalāl industries and therefore giving imputes for real economic growth. With only three countries having reported Islamic banking assets, the region’s Islamic total banking assets were reported at USD 285 million in 2022.

In the next ten years, we expect significant growth and development in the Islamic finance industry in the region, driven mainly by the Islamic banking sector and the Şukūk asset class. The growth of financial intermediation and an estimate of the change in the share of Islamic finance in the financial sector structure was used to project the increase in Islamic finance assets in the region. This approach assumes an increase in Islamic banking assets to the level of USD 2.5 billion in 2028 and USD 6.3 billion in 2033. Given the favourable demographics, strong economic growth, and the substantial size of the banking industry in each of the five Central Asian nations, Kazakhstan is expected to be the leader, followed closely by Uzbekistan. The region’s Şukūk market is also expected to witness significant expansion: the baseline forecasts suggest that Şukūk market is anticipated to grow to USD 2.05 billion by 2028 and USD 5.6 billion by 2033.

Figure 4.1.1: Projected Islamic Finance Assets in Central Asia



Source: IsDBI – LSEG analysis, authors’ estimates

In the next ten years, we expect significant growth and development in the Islamic finance industry in the region, driven mainly by the Islamic banking sector.



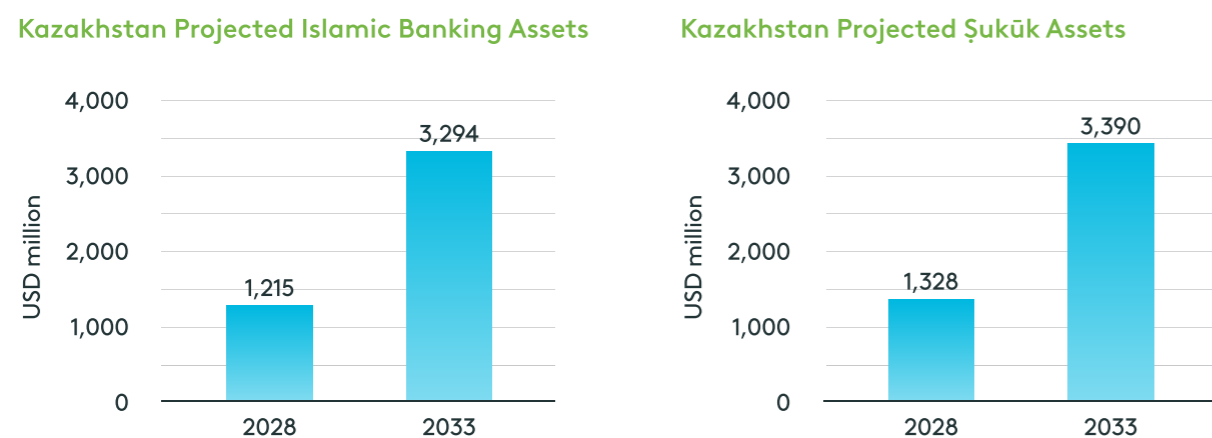
4.2 Kazakhstan

Kazakhstan has a diverse population of different Asian ethnic groups totalling 19.8 million as of December 2022, with the 15 to 64 age group accounting for 62% of the population, and those under 25 accounting for nearly 42%. Muslims comprise 70% of the total population. According to the World Bank Financial Inclusion indicator, 19% of the country's population over 15 years of age did not have a bank account in 2021, the lowest in the region, and 5% of those said this was for religious reasons. The survey also showed that 40% of the adult population of Kazakhstan saved money, but just 19% saved at financial institutions. These findings present a large, untapped opportunity for the Islamic finance industry. For example, according to the Astana International Finance Center, market demand for Islamic Deposits in a retail segment in Kazakhstan is up to approximately 6.3 billion USD (AIFC, 2024a).

Although the Islamic banking sector accounted for less than 1% of total banking industry assets at the end of 2023, the country is building on strong foundations to develop its Islamic finance industry, as can be seen by the introduction of the Islamic Finance Master Plan for the Republic of Kazakhstan 2020-2025 prepared for the AIFC with technical assistance from the IsDB (AIFC, 2020). Developing the Islamic banking sector is expected to strengthen the country's domestic financial system by mobilizing locally available liquidity, in line with the government's aim to develop a market-driven rather state-supported economy. The key pillars covered under the Master Plan include the internationalisation of the AIFC; Islamic banking; an Islamic capital market; takāful; Islamic non-banking institutions; Islamic social finance; FinTech; the Ḥalāl sector; and Islamic finance education and training.

The two sectors most likely to drive Kazakhstan's Islamic finance industry forward are Islamic banking and Ṣukūk. Given this as well as the recent initiatives towards developing the industry, the prospects for the industry's development, as well as the high demand for Islamic finance products (AIFC, 2024a), the country's Islamic banking sector is projected to grow to USD 1.2 billion by 2028 and USD 3.3 billion by 2033 under the baseline scenario. For the Ṣukūk asset class – which is more active as more sovereigns and corporates have issued Ṣukūk globally over the past few years, something which Kazakhstan could observe and learn from – its total value is projected to reach USD 1.3 billion by 2028 and USD 3.4 billion by 2033.

Figure 4.2.1: Projected Islamic Finance Assets in Kazakhstan



Source: IsDBI – LSEG analysis, authors' estimates

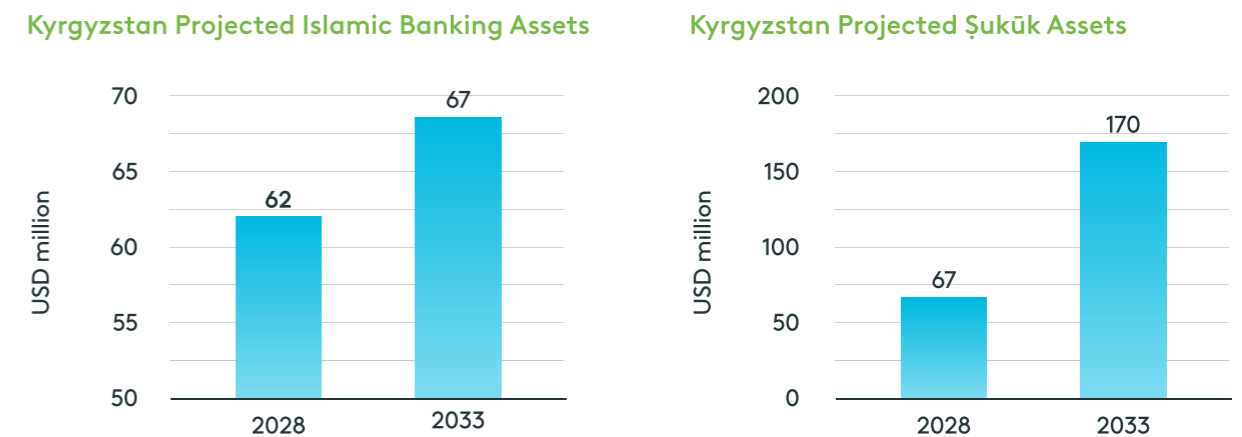
4.3 Kyrgyzstan

The Kyrgyz Republic had a population of 7.0 million as of December 2022, of which 90% are Muslim. In addition, 58% of the population falls within the 15-64 age group. Financial inclusion stands at 41%, as measured by the share of the adult population that holds accounts with financial institutions. Around 8% cited religious reasons for not having such accounts. Around 32% of the adult population saved money, although just 7% was with a financial institution.

The country's central bank set a targeted indicator of 5% share of the Islamic banking sector in its strategic document for the 2013-2027 period. According to the National Bank of the Kyrgyz Republic (NBKR), previously conducted studies and surveys have shown a high unmet demand for Islamic finance in the small and medium business sector. In 2022, the Islamic banking sector's assets accounted for just 1.5% of total banking sector assets, despite the country's proportionately large Muslim population. This suggests that there is great potential for the industry to develop. In 2023, government approved the concept for the development of the Islamic economic platform in the Kyrgyz Republic for 2023-2027, with the aim of making the country a regional centre for Islamic finance. It was also reported in March 2023 that there were plans to launch the country's first Islamic investment bank (Daryo, 2023).

Projections for Kyrgyzstan's Islamic banking sector assume that sector will experience substantial growth, reaching USD 62 million by 2028 and USD 67 million by 2033. Alongside the growth in Islamic banking, the Ṣukūk market in Kyrgyzstan is also expected to witness significant development. The outstanding value of Ṣukūk is projected to grow to USD 67 million by 2028 and USD 170 million by 2033.

Figure 4.3.1: Projected Islamic Finance Assets in Kyrgyzstan



Source: IsDBI – LSEG analysis, authors' estimates



4.4 Tajikistan

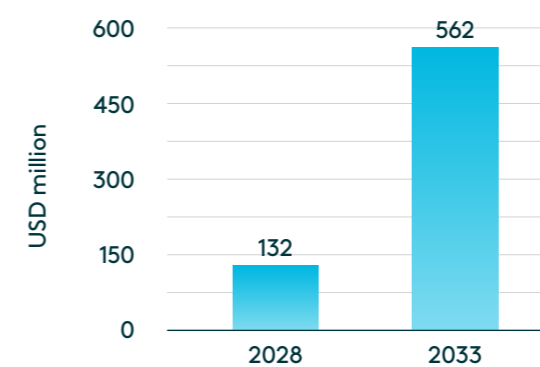
Tajikistan has a population of 10.1 million as of the end of 2022, of which 62% fall within the 15-64 working age bracket and almost 36% are younger than working age population. The Muslim share of the population is 97%. The World Bank reported that 39.5% of the adult population holds accounts with financial institutions, with 6% saying they had no such account for religious reasons. Around 18% of the adult population saved money, although just 1% saved with financial institutions, suggesting a sizeable untapped opportunity.

Given these statistics, Islamic banking looks to have huge potential to grow from the 1.1% share of the country's total banking sector at the end of 2023. Alif Bank, an Islamic FinTech unicorn based in Tajikistan, saw 170% growth in its assets in 2022 from 2021 (Alif Bank, 2022). The total assets of another leading Islamic bank, Tawhid Bank, reached in 2023 about USD 22.3 million, representing a 14% increase from the previous year. According to the National Bank of Tajikistan, as of July 31, 2024, the assets of Islamic credit institutions increased by 28.4% and profits increased 1.5 times compared to the same period in 2023. One driver for the development of Islamic finance in the country was the establishment of the Consultative Council for Islamic Banking Services by the National Bank of Tajikistan in 2017. In addition, the country's National Financial Inclusion Strategy 2022-2026, which was developed with the support of the International Finance Corporation, includes diversifying financial services partly through Islamic financing (National Bank of Tajikistan, 2022).

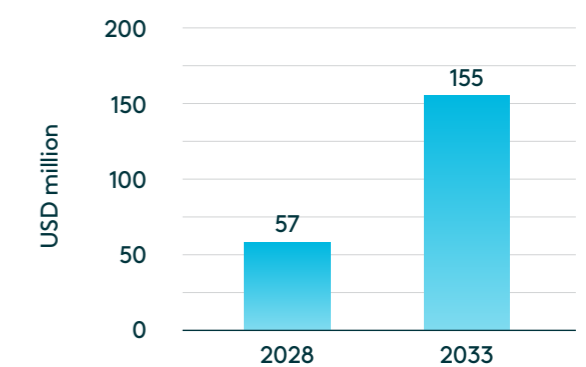
Tajikistan's Islamic banking assets are forecast to grow from USD 132 million in 2028 to USD 562 million in 2033. The Şukūk market is also projected to flourish with outstanding Şukūk reaching USD 57 million in 2028 and USD 155 million in 2033.

Figure 4.4.1: Projected Islamic Finance Assets in Tajikistan

Tajikistan Projected Islamic Banking Assets



Tajikistan Projected Şukūk Assets



Source: IsDBI – LSEG analysis, authors' estimate

4.5 Turkmenistan

Turkmenistan is the smallest Central Asian nation in terms of population, with 6.4 million people. According to a 2020 estimate, 93% of the population follows Islam. The World Bank's 2017 Global Findex Database showed that 41% of adults held accounts with financial institutions. While 51% of adults saved money, just 5% did so with a financial institution.

In Turkmenistan, the Islamic finance industry is still in its nascent stage, with no Islamic financial institution currently operating in the country. However, there is a strong demand for Islamic financial services, given the high Muslim population. Efforts have been made to raise awareness, such as the Islamic trade finance workshop organized by the International Trade Finance Corporation (ITFC), a member of the IsDB Group, in 2022. The workshop, which focused on operational aspects of Islamic banking, attracted numerous local financial institutions, indicating substantial interest in the industry. With a mix of state, joint-stock, and overseas banks operating in Turkmenistan, the presence of Islamic windows could potentially benefit the country's financial sector. Due to data inaccessibility, forecasting future Islamic finance assets in Turkmenistan remains challenging.

In Turkmenistan, the Islamic finance industry is still in its nascent stage, with **no Islamic financial institution currently operating in the country.**

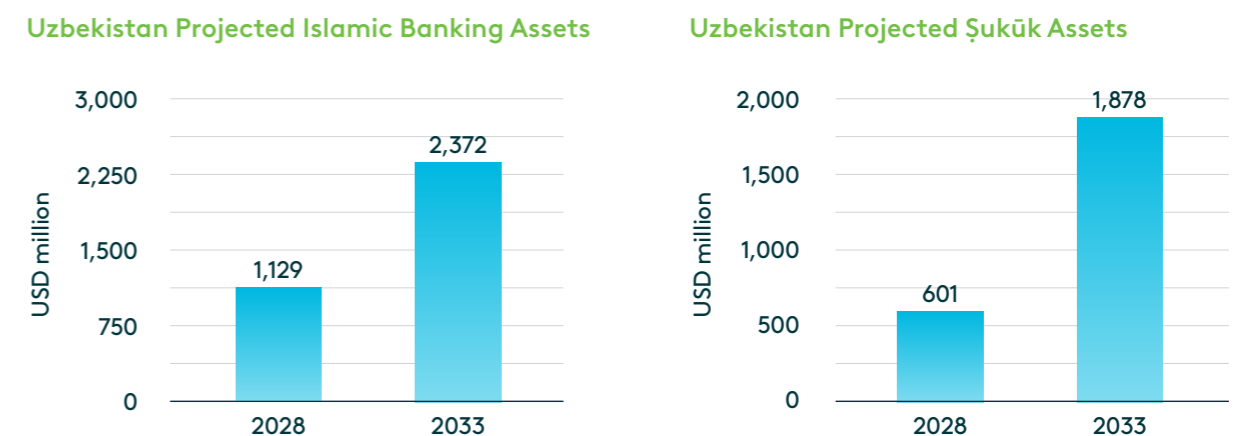
4.6 Uzbekistan

Uzbekistan's population numbers 36.06 million, accounting for 45% of the entire Central Asia region. Around 71% of Uzbekistanis are in the 15-64 age group and 88% are Muslim. The World Bank reported that 44% have accounts at financial institutions, and 16% do not for religious reasons. While 28% saved money, only 3% saved at a financial institution.

While data for Uzbekistan's Islamic finance industry are not publicly available, the country has sizeable potential to serve its large Muslim population. The government is planning to launch the Tashkent International Financial Centre, a special free economic zone that would support development of the country's Islamic finance industry. In addition, in its 2030 strategy, as part of reforms of the banking system, the country plans to introduce criteria and procedures for Islamic financing in at least three commercial banks (The Government portal of the Republic of Uzbekistan, 2024). Also, the Financial Sector and Banking Working Group at the country's Foreign Investors Council, which aims to increase the share of private banks in the banking sector to 60% by 2025, is proposing to dedicate a subgroup for the creation of an Islamic banking roadmap, including Islamic banking law (FIC, 2024).

Uzbekistan's Islamic finance assets are also projected to grow to USD 1.1 billion in 2028 and USD 2.4 billion in 2033. The Şukūk market is anticipated to thrive, with outstanding Şukūk expected to total USD 601 million in 2028 and USD 1.9 billion in 2033

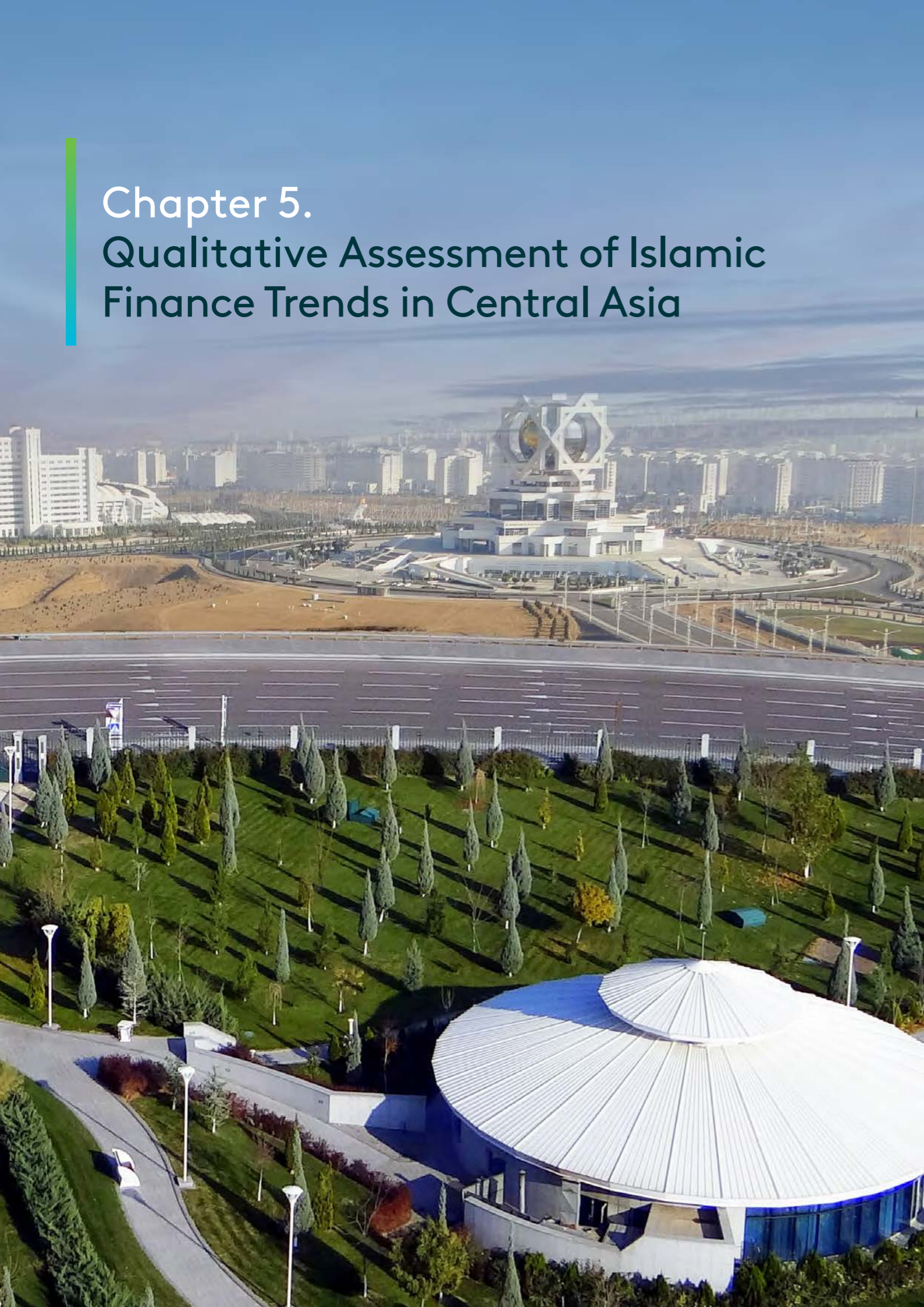
Figure 4.6.1: Projected Islamic Finance Assets in Uzbekistan



Source: IsDBI – LSEG analysis, authors' estimates

Chapter 5.

Qualitative Assessment of Islamic Finance Trends in Central Asia



5.1 Overview

A. Sectors to Focus on

Over the next 5-10 years, as Central Asian countries continue to build on previous initiatives, momentum should build towards strengthening the fundamentals underpinning their nascent Islamic finance ecosystems. These could include a more developed Islamic banking landscape with more varied products and services on offer, thriving Islamic capital markets with greater *Shukūk* and *Sharī'ah*-compliant equity issuances, and growing markets for Islamic asset management and Islamic FinTech.

Beyond these core elements, Central Asian jurisdictions may also look to eventually incorporate wider developments from the evolution of Islamic finance in leading jurisdictions such as Malaysia and the UAE, as well as market practices from large Islamic economies such as Saudi Arabia and Indonesia. Some of these developments would likely include a move towards greater integration of Islamic finance with ESG and sustainability practices; linkages with the *halāl* economy sectors such as *halāl* food, Muslim-friendly travel and tourism, and modest fashion; and the deepening of Islamic banking products and services and local Islamic capital markets so that Central Asian Islamic banks can increase their domestic market shares and Central Asian countries can tap foreign investments into their burgeoning economies. An example is Malaysia, whose Securities Commission seeks in its Capital Markets Masterplan 3 (2021-2025) to develop “a capital market that is more relevant, efficient and diversified” (Securities Commission Malaysia, 2021).

Given the still relatively novel nature of Islamic finance in Central Asia, stakeholders could prioritise enabling both a broader and deeper market that more fully applies the sectoral and functional aspects of Islamic finance. As a sector, the Islamic finance industry in these five countries will need to develop a wide range of products and services that can serve *Sharī'ah*-sensitive corporates and investors looking to Central Asia for business and investment opportunities. Products such as **working capital** (e.g., *murābahah*-based contracts), **leasing** (*ijārah* structures), and various **trade finance** instruments (such as *Sharī'ah*-compliant letters of credit) may be needed to cater to these corporates' needs in Central Asia. Also, *Shukūk* could play a key role in attracting foreign investors seeking opportunities in Central Asia. For *Shukūk* to flourish in the region, a number of enabling factors will need to be realised, such as a level playing field in tax laws and capital markets regulation, more benchmark sovereign *Shukūk* issuances, and the subsequent fostering of a corporate *Shukūk* market in Central Asia.

B. Key Ecosystem Players

Some of the key enabling **ecosystem** players include legal and regulatory enablers, professional service firms, financial institutions, and supporting institutions. The table below provides more detail on these types of ecosystem players along with examples.

Table 5.1.1: Ecosystem Enablers for Islamic finance in Central Asia

Ecosystem Category	Sub-Types & Examples
Regulatory Enablers	<ul style="list-style-type: none"> Multilateral development banks <ul style="list-style-type: none"> e.g., Islamic Development Bank (IsDB), World Bank, Eurasian Development Bank (EDB) Supranational regulators <ul style="list-style-type: none"> e.g., Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), Islamic Financial Services Board (IFSB) National regulators in developed Islamic finance jurisdictions <ul style="list-style-type: none"> e.g., National Bank of Kazakhstan, Central Bank of the Republic of Uzbekistan, Agency for Regulation and Development of the Financial Market of the Republic of Kazakhstan e.g., regulators from developed Islamic finance jurisdictions such as Bank Negara Malaysia, Saudi Central Bank, and the Central Bank of the UAE
Professional Services	<ul style="list-style-type: none"> Lawyers <ul style="list-style-type: none"> e.g., magic circle law firms e.g., law firms from OIC countries Shari'ah scholars and advisors <ul style="list-style-type: none"> e.g., individual scholars e.g., Shari'ah advisory firms Consultants <ul style="list-style-type: none"> e.g., "Big 4" consulting firms such as EY, Deloitte e.g., Islamic finance specialists such as Islamic Finance Advisory and Assurance Services
Financial Institutions	<ul style="list-style-type: none"> Islamic banks <ul style="list-style-type: none"> e.g., GCC Islamic banks such as Al Rajhi, Dubai Islamic Bank, and Qatar Islamic Bank e.g., Southeast Asian Islamic banks such as Maybank Islamic, CIMB Islamic, and Bank Syariah Indonesia (BSI) Venture capital firms <ul style="list-style-type: none"> e.g., global firms such as 500 Global e.g., Islamic economy-focused firms such as Gobi Partners Sovereign wealth funds <ul style="list-style-type: none"> e.g., Samruk-Kazyna, Kazakhstan National Fund Islamic FinTechs <ul style="list-style-type: none"> e.g., Alif Bank (Tajikistan), Iman (Uzbekistan)
Supporting Institutions	<ul style="list-style-type: none"> Research institutions <ul style="list-style-type: none"> e.g., Islamic Development Bank Institute (IsDBI) Education & training institutes <ul style="list-style-type: none"> e.g., International Centre for Education in Islamic Finance (INCEIF), Bahrain Institute of Banking & Finance (BIBF) Islamic finance industry associations <ul style="list-style-type: none"> e.g., Council of Islamic Banks and Financial Institutions (CIBAFI)

Source: IsDBI analysis

5.2 Improving Islamic Finance in Central Asia

A. Funding Prospects

According to our estimates, the GDP of Central Asian countries will increase by 5.2% in 2024, following a growth of 5.3% in 2023. Economic growth will be supported by domestic sources and improved export prospects. Kazakhstan's economy is expected to grow by an average of 5% in 2024-2025, based on the government's initiatives to diversify the industrial sector. According to Strategy Kazakhstan-2050, one of the key policy documents, the country aspires to become one of the Top-30 most developed countries of the world by 2050. High investment demand and growth in exports, primarily of base metals, will support the economies of Uzbekistan, the Kyrgyz Republic, and Tajikistan. The Central Asian countries are projected to grow slightly above 5% in 2024- 2025 (Vinokurov et al., 2024).

Additional imputes to long term growth in Central Asian countries lie in the **Middle Corridor**, a Trans-Caspian trade route enabling multi-modal land and sea connectivity that effectively connects China with Europe via Kazakhstan, indirectly connecting them with neighbouring Central Asian countries bordering Kazakhstan such as Kyrgyzstan and Uzbekistan (Fanger, 2023). Other factors boosting the economic growth outlook in Central Asia include China's Belt and Road Initiative (BRI), the EU's Global Gateway strategy (Fanger, 2023) and Eastern Route of International North – South Transport Corridor (INSTC) – each these transport corridors involve Central Asia as a key component into regional and global trade system.

These positive economic fundamentals, along with growing interest in Islamic finance products and services in Central Asia, suggest that the prospects for Islamic finance in Central Asia are also promising. More specifically, they also give reasonable cause for optimism when evaluating international funding prospects for Islamic banks and **Şukūk** issuances in Central Asia.

B. The Roles of MDBs

Multilateral development banks (MDBs) play a crucial role in fostering and financing sustainable growth in Islamic banking penetration in emerging Islamic finance jurisdictions, including Central Asia. For example, the Islamic Development Bank (IsDB) has been at the forefront of such developments and efforts via a large number of projects. As the table below illustrates, the IsDB has completed 276 projects in the five Central Asian nations to date, with another 160 projects being active. Total IsDB funding to date in Central Asia has reached **USD 7.78 billion**.

Other MDBs are also active in building the ecosystem for Islamic finance and other types of finance, such as infrastructure finance. These development banks include the Eurasian Development Bank (EDB), the Asian Development Bank (ADB), and the Asian Infrastructure Investment Bank (AIIB). For example, a good case is the ADB's ongoing technical assistance project "Islamic Finance for Inclusive Growth", aiming to develop Islamic finance in Kazakhstan, Kyrgyzstan, and Tajikistan (also Afghanistan and Pakistan), promoting legal and regulatory reforms, financial inclusion, economic growth, and poverty reduction through capacity building, vocational training of governmental and regulatory participants, and regulatory support, encouraging the growth of Islamic finance products and services, development of additional monetary instruments, etc. (Jimenez et al., 2024)

The EDB announced in October 2023 that it planned to become a significant regional player in the Islamic finance industry, working on the relevant institutional and administrative solutions in order to finance investment projects in Central Asia, attract investments, and potentially draw the attention of global investors and set a benchmark for its member states, issuing Shari'ah-compliant debt instruments (Haidar, 2023).

MDBs are also working together on Central Asia. For example, the IsDB and AIIB held a dialogue session with key stakeholders in March 2024 to discuss how to increase regional economic cooperation and integration (IsDB, 2024c). Taken together, these are welcome developments for sustainable growth in Islamic banking penetration in Central Asia, along with the natural synergies between Islamic and infrastructure finance and the obvious role that banks can play in financing infrastructure.

Such efforts by MDBs are already facilitating promising inroads into Islamic banking in Central Asia. For example, a 2024 study by CSQ Law supported by the IsDB Institute has projected the new volume of Islamic deposits in Kazakhstan at **2.8 trillion tenge (USD 6.3 billion)**. This figure comprises an estimated 1.9 trillion tenge (USD 4.2 billion) in new deposits along with 924 billion tenge (USD 2 billion) in deposits that can be converted from conventional into Islamic deposits (AIFC, 2024b). The study estimated this market demand based on a survey of close to 13,000 participants from Kazakhstan that included 350 legal entities and more than 12,000 individuals. It also estimated immediate market demand for Shukūk in Kazakhstan from individual investors to be 46 billion tenge (USD 103 million) annually (AIFC, 2024c).

Table 5.2.1: IsDB Projects and Funding in Central Asia

Country	Total Projects	Completed Projects	Active Projects	Total IsDB Group Funding (USD billion)
Kazakhstan	74	57	17	1.656
Kyrgyzstan	82	63	19	0.554
Tajikistan	105	72	33	0.825
Turkmenistan	33	17	16	1.387
Uzbekistan	168	73	95	3.974
Central Asia Total	462	282	180	8.396

Source: IsDB Group (data is from commencement of operations to 30 June 2024)

C. The Role of International Islamic Banks

International Islamic banks from more mature Islamic finance jurisdictions such as the Persian Gulf countries and Southeast Asia can help build capacity in Central Asian Islamic banking ecosystems. Although Islamic banking is still at a very early stage in most Central Asian countries, there are some examples of international Islamic banks operating in Kazakhstan. For instance, **Al Hilal Bank**, owned by Abu Dhabi-based ADCB, has operated in Kazakhstan since 2010. As of January 1, 2024, it has an asset base of USD 395 million and branches in Almaty, Astana, and Shymkent, which offer Shari'ah-compliant products to both individual and corporate customers (Rafiq, 2023). **Zaman Islamic Bank**, Kazakhstan's second Islamic bank, started operations in 2017 after converting from a conventional bank. It had USD 55 million in assets at the beginning of 2024, with branches in Almaty, Astana, and Ekibastuz (Rafiq, 2023).

Apart from providing banking products and services, international Islamic banks – along with professional services firms such as international law firms, Shari'ah advisory firms, and global consultancies – can enable knowledge transfers in Central Asian countries to enhance the levels of Islamic finance technical expertise they can draw upon. Further down the line, once strong legal, regulatory, and policy foundations are in place, Central Asian countries may wish to access capital via sovereign Shukūk issuances and grow their corporate Shukūk markets. The expertise of international Islamic banks will be pivotal in helping successfully execute such issuances. This type of institution-level support would complement the more high-level funding and policy-oriented work that MDBs currently provide in Central Asia.

D. The Role of Central Banks and Governments

Central banks and governments in Central Asia have a key role in facilitating the development of Islamic finance in those countries. Apart from legal, regulatory, and general policy, there are at least two other key aspects where their efforts are crucial. First, **investment promotion** by government bodies is vital in increasing awareness among international investors of the opportunities in Central Asia that these global investors can realise, for example by highlighting specific sectors and industries and facilitating connectivity on the ground with local companies and organisations. It's also important to provide legal framework for banks to open "Islamic window", and enable mechanisms and methodologies for proper fiscal administration of these operation, as well as recognition some operations in commodity platforms as Islamic banking operation. Second, Central Asian central banks can help improve aspects of the financial ecosystem by providing central bank **liquidity management tools**. Given that most banking in Central Asia remains conventional in nature, providing Shari'ah-compliant liquidity facilities is key to building the market for Islamic banking. One such example of a facility provided within a conventional banking system already exists in the UK, where the Bank of England introduced an Alternative Liquidity Facility to enable UK Islamic banks to hold non-interest-bearing deposits with it (Bank of England, 2021). Perhaps this model is worth considering in the Central Asian context.

5.3 Recommendations and Strategic Considerations

A. For Governments

- **Create the enabling legal, regulatory, and policy environment:** Islamic finance has yet to realise its potential in Central Asia, and an important barrier to this growth is the lack of enabling legal, regulatory, and policy conditions across all five countries. Kazakhstan is probably the most advanced Islamic finance market in the region due to its initiatives in these areas, such as the Astana International Financial Centre (AIFC). Other Central Asian countries can emulate and adapt Kazakhstan's initiatives and success stories to develop their Islamic banking and Şukūk markets. Conversely, countries such as Kazakhstan and Kyrgyzstan that already have some of these ecosystem factors in place can learn how to better foster national Islamic FinTech ecosystems, building on success stories in other Central Asian nations such as Alif Bank and Iman.

At the same time it should be useful for Kazakhstan to develop an Islamic deposit guarantee system and to allow conventional banks to open "Islamic windows" with Islamic finance products.

- **Address talent shortages:** For Islamic banks, Şukūk, and other Islamic finance markets such as Islamic asset management and Islamic FinTech to grow, Central Asian countries need to develop talent pipelines and thereby reduce shortages of qualified talent. For instance, universities in these Central Asian countries should introduce educational programs that develop tertiary-level qualified talent, e.g., by offering undergraduate or postgraduate degrees or applied certifications in Islamic finance. These universities could learn from the experience of leading universities in Islamic finance globally, such as INCEIF and Durham University Business School. Moreover, governments in these countries could help support such programs.
- **Facilitate trade relationships and corridors with neighbouring countries:** Although strategically placed between China, Russia, and Europe, the five Central Asian nations are disadvantaged by geography in one important respect: they are all landlocked nations (Uzbekistan is double-landlocked in that it is surrounded by other landlocked countries). Consequently, connectivity via trade corridors with adjacent countries is critical to the long-term economic viability and growth of these nations. Central Asian governments can help foster such ties to drive win-win cross-regional outcomes.

B. For Investors

- **Understand that Islamic banking and Şukūk in Central Asia are growing opportunities:** Given the healthy economic fundamentals of Central Asian countries and rising pent-up demand for Islamic financial services, as shown for example by the USD 6 billion Islamic deposits potential in Kazakhstan and near USD 100 million projected annual demand for Şukūk in Kazakhstan, Islamic banking and Şukūk are unutilized opportunities waiting to be tapped, as revealed in the AIFC's Kazakhstan Islamic Finance report released in March 2024 (AIFC, 2024a). Although Kazakhstan's level of Islamic finance development may not represent the state of progress in

the other four Central Asian countries, the other four countries are also working on improving their Islamic finance ecosystems, as mentioned elsewhere in this report.

- **Support investing in regional Islamic economy startups:** There are a few examples of established startups in Central Asia that are focused on areas in the Islamic economy like Islamic FinTech and digital banking such as Alif Bank and Iman. More of these success stories are needed, and there is ample scope for investors to uncover profitable opportunities by backing emerging startups that are regionally based or focused and which have an Islamic FinTech or Islamic economy focus (e.g., segments such as ḥalāl food, Muslim-friendly travel and tourism, modest fashion). These investors could include regional or global angel investors and venture capital firms.
- **Consider investing in Sharī'ah-compliant ESG activities and technology funds:** Globally, investors in other countries, including the OIC nations, are keen to invest in ESG activities and technology funds (DinarStandard, 2023). With the increasing urgency of ESG concerns due to factors such as climate change and the continued rise of technologies such as artificial intelligence (AI), there is a good opportunity for investors to back the creation of regional success stories and champions in these market spaces.
- **Collaborate and build relationships with regional MDBs with an active presence in Central Asia** in order to gain access to quality local projects (public and private), significant investment experience and deep expertise of regional development banks.

C. For Businesses

- **Consider sourcing Sharī'ah-compliant funding:** Sharī'ah-compliant funding is scarce in most Central Asian countries. However, the situation is gradually changing and Sharī'ah-sensitive businesses in Central Asian markets can look to regional Islamic banks and regional and global investors to source the funds they need to grow their businesses.
- **For SMEs, consider these sources:** Given that businesses may vary widely in their needs and development stages, there is no single solution that will apply. For example, SMEs in Central Asia will likely need working capital facilities and may be better suited to seeking Sharī'ah-compliant funding from domestic Islamic banks or government agencies that have a mandate to support the SME segment.
- **For larger companies, consider these sources:** Conversely, larger companies may be interested in tapping corporate banking solutions or issuing corporate Şukūk. Both of these solutions are in the early stages still in Central Asia, but the situation is fluid.

Appendix: Methodology of Islamic Finance Assets Projection

1. Horizon of Projection

Medium-term – five years (2028) and long-term – ten years (2033).

2. Forecasting Components (Indicators)

When projecting the baseline growth of Islamic finance, two components of the industry are most likely to power it forward given their large share of the industry's total assets:

1. Islamic banking, which had 72% of global Islamic finance assets in 2022, according to the ICD-LSEG Islamic Finance Development Report 2023; and
2. Şukūk, the second largest contributor of Islamic finance assets with a 17% share.

3. Data Collection

Data used for Islamic finance assets projection was sourced from multiple reliable sources, including:

1. Global Islamic financial institutions (e.g. AAOIFI, IFSB, ...); Central banks and regulators of countries with significant Islamic finance activity (e.g. Malaysia, UAE, Saudi Arabia); Industry reports from consulting firms and market research organisations (e.g. McKinsey, Deloitte); Financial statements of Islamic banks and non-banking financial institutions.
2. Statistics of national agencies of Central Asia and international institutions:
 - Demographic data by country, including population, population growth rate, life expectancy and age structure,
 - Historical data on banking sector assets in each country,
 - Historical data on Islamic banking assets in Kazakhstan, Kyrgyzstan and Tajikistan.
 - Average Şukūk value to banking assets as well as average Şukūk value to GDP as a benchmark for Central Asian countries.

4. Projection Methodology

- a. Population growth assessment was based on estimates of demographic change in each country based on United Nations estimates in World Population Prospects 2024 (UN, 2024)
- b. Estimation of demand for financial intermediation services in the countries of the region
- c. Expert estimates of changes in the share of Islamic finance in the total demand for financial services
- d. Extrapolation of the growth of Islamic finance

5. Approaches and Assumptions Used for Projections of the Assets:

- a. We assume that growth in the Islamic banking and Şukūk sectors is highly correlated with the demand for financial intermediation services.
- b. We assume that Şukūk sector growth will coincide with the growth dynamics of Islamic banking.
- c. In estimating the demand for banking intermediation services is estimated on the basis of growth in economic activity and price movements. An additional important factor is the increase in the working-age population due to the leveraging of the demographic dividend – increasing the share of the population of working age. We assume an increase in the share of Islamic finance in the structure of financial intermediation services in the conditions of increasing share of Muslim population in the Central Asia countries, as well as the readiness of part of the population to switch from traditional finance to Islamic finance if there is a sufficient supply of it (AIFC, 2024c). The experience of other countries with predominantly Muslim populations and a mixed type of financial system indicates an increase in the share of Islamic finance in the structure of bank assets. A good peer country would be Turkey – a country located in the region with a high share of Muslim population and a relatively developed conventional financial system at the time of the emergence of Islamic finance. The share of Islamic finance evolved from 1.1% in 2001 to 3.6% in 2013 and remained at this level. We have calculated the growth of the Islamic finance assets for three countries – Kazakhstan, Tajikistan, and Kyrgyzstan – where historical data on Islamic banking assets are available.
- d. In order to verify the reliability of the obtained results, we extrapolated the growth of Islamic banking assets for the three countries mentioned above (Kazakhstan, Kyrgyzstan, Tajikistan). We calculated the compound annual growth rate (CAGR) for the available periods where:

EV = Ending value

BV = Beginning value

n = Number of years

- e. We then presumed that the same growth rate should be applied for the forecasts of five years and ten years in a baseline scenario.

$$\text{CAGR} = \left(\left(\frac{\text{EV}}{\text{BV}} \right)^{\frac{1}{n}} - 1 \right) * 100$$

5. f. Given the relative similarity of the results obtained by both methods, we decided to use the results of extrapolation method for the purposes of the paper in order to reduce the effect of the judgments used in assessing the change in the share of Islamic financing in the structure of banks' assets.
- g. For Uzbekistan, where there is no historical data on Islamic banking or *Shukūk* assets, we used the proxy data of neighbouring countries. The share of the Muslim population in the total population in Uzbekistan is almost the same as in neighbouring countries. Thus, we took, on average, the share of the Islamic banking assets in the total banking sector in those three countries (Kazakhstan, Tajikistan, and Kyrgyzstan), and used it in calculating the share of Islamic banking assets in the total banking sector of Uzbekistan. To find the total banking sector's assets by 2028 and 2033, we have calculated the CAGR of the total banking sector in Uzbekistan for 2018-2023. Then we applied the same CAGR for estimation of the total banking assets for 2028 and 2033. Developed Islamic finance markets' statistics are used as a proxy to determine the appropriate share of *Shukūk* assets in the total banking sector assets, which is what the Central Asian nations will strive to achieve within ten years if they follow the Islamic finance development footsteps of these developed markets. Such data are sourced from LSEG's Islamic Finance Development Indicator 2023.
- h. Data from recent surveys in Central Asian countries indicate that the growth potential of Islamic finance may be greater, as a part of the Muslim population does not use non-Shari'ah compliant banking services. This may be a potential for additional expansion of financial intermediation services in Central Asian countries.



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Research on the EDB Website



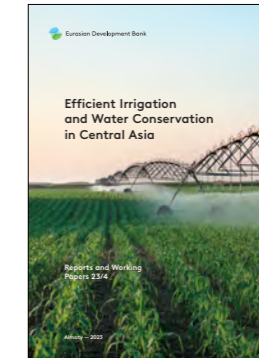
Macroeconomic Outlook (RU/EN)
Macroeconomic Outlook 2024–2026
 The EDB forecasts that the aggregate GDP of the Bank’s member countries will grow by more than 3% in 2024. The economic growth rates of the Eurasian region will be higher than the global average.



Report 24/7 (RU/EN)
Capital in Multilateral Development Banks
 This paper covers the whole ‘MDB family’ of institutions but highlights regional and subregional MDBs because of their specifics of raising shareholders’ capital. The study discusses seven standard and novel options for increasing capital.



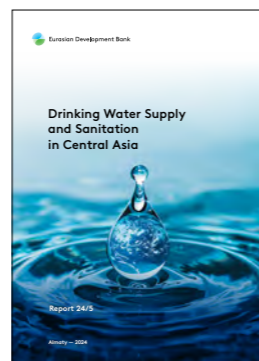
Report 23/5 (RU/EN)
EDB Monitoring of Mutual Investments — 2023
 Eurasian countries’ FDI stock reached USD 48.8 billion by mid-2023, following a 5.4% increase in 2022 and with continued growth in 2023.



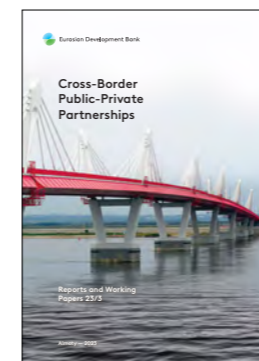
Report 23/4 (RU/EN)
Efficient Irrigation and Water Conservation in Central Asia
 A new EDB study outlines ten practical steps for preserving irrigated land potential and promoting water conservation. The list includes four recommendations for adoption at the regional level and six at the national level.



Report 24/6 (RU/EN)
The Eurasian Transport Network
 The report examines ten system elements of the Eurasian transport framework concept. Among them are the formation of a transport crossroads in Central Asia, priorities for intraregional transport connectivity, an impetus for realizing the agro-industrial potential of the countries of the region, and improvement of soft infrastructure.



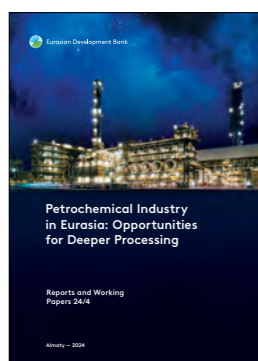
Report 24/5 (RU/EN)
Drinking Water Supply and Sanitation in Central Asia
 In Central Asia, 10 million people do not have access to safe drinking water. Given the priority importance of drinking water for public health and the scale of the challenges, a comprehensive approach is required in the region. A new EDB report presents a set of practical steps that shape such an approach.



Report 23/3 (RU/EN)
Cross-Border Public-Private Partnerships
 The report outlines the criteria and scope of cross-border PPP projects, evaluates their potential for fostering cross-border infrastructure development in the EAEU, Central Asia, and the South Caucasus, and suggests guidelines for the successful implementation of cross-border PPPs in the region.



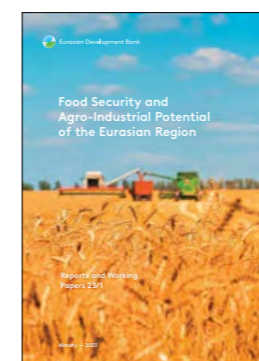
Report 23/2 (RU/EN)
Global Green Agenda in the Eurasian Region. Eurasian Region on the Global Green Agenda
 The report provides a comprehensive analysis of the challenges and prospects for lowcarbon transition in Eurasia, covering EAEU countries, Tajikistan, and Uzbekistan.



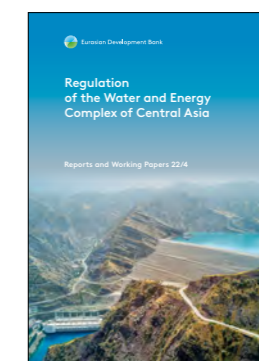
Report 24/4 (RU/EN)
Petrochemical industry in Eurasia: Opportunities for Deeper Processing
 The analytical report uses a balance approach to assess the production and export potential of the petrochemical complex of the Eurasian region (Armenia, Belarus, Kazakhstan, Kyrgyzstan, Russia, Tajikistan, Turkmenistan, Uzbekistan) in the perspective up to 2035.



Report 24/3 (RU/EN)
Infrastructure in Eurasia: short-term and medium-term trends
 The EDB’s report highlights ten important short- and medium-term investment and institutional trends in the region’s energy, transportation, logistics, water supply and telecommunications sectors.



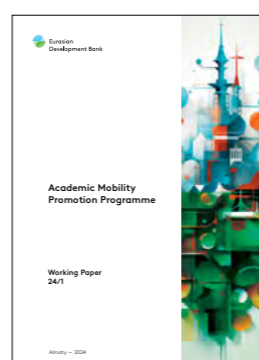
Report 23/1 (RU/EN)
Food Security and Agro-Industrial Potential of the Eurasian Region
 Based on the balance approach, the report analyses the production, resource, and export potential of the agro-industrial complexes of the EAEU countries, Tajikistan, and Uzbekistan for the period until 2035.



Report 22/4 (RU/EN)
Regulation of the Water and Energy Complex of Central Asia
 The report scrutinises historical data and international experience to suggest five institutional solutions for effective regulation and development of Central Asia’s water and energy complex that would benefit all countries of the region.



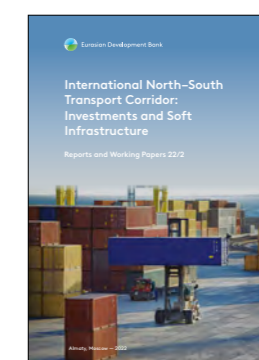
Report 24/2 (RU/EN)
Economic Cooperation in Eurasia: Practical Solutions
 The EDB’s report “Economic Cooperation in Eurasia: Practical Solutions” contains a “menu” of pragmatic applied solutions that can be enabled relatively fast and with flexible configurations among participating countries aimed at fostering mutually beneficial economic cooperation among Eurasian countries.



Report 24/1 (RU/EN)
EDB Monitoring of Mutual Investments — 2023
 Eurasian countries’ FDI stock reached USD 48.8 billion by mid-2023, following a 5.4% increase in 2022 and with continued growth in 2023.



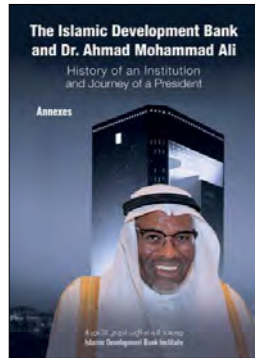
Report 22/3 (RU/EN)
The Economy of Central Asia: A Fresh Perspective
 The report provides a renewed perspective on Central Asia as a large, dynamic and promising economic region and analyses its current structural changes and major growth areas.



Report 22/2 (RU/EN)
International North-South Transport Corridor: Investments and Soft Infrastructure
 The study assesses the investment potential of the INSTC, identifies barriers to its development and provides recommendations on how to eliminate them.



IsDB Institute Publications



The Islamic Development Bank and Dr. Ahmad Mohammad Ali: History of an Institution and Journey of a President

This book chronicles the history of the Islamic Development Bank and the leadership of its first president, Dr. Ahmad Mohammad Ali, highlighting key milestones and his impactful initiatives.



Celebrating IsDBI at 40

This report commemorates 40 years of the Islamic Development Bank Institute's contributions, reflecting on its milestones, impact, and ongoing efforts in advancing Islamic finance.



Annual Report 2023

The report showcases the IsDB Institutes key achievements in major functional areas including research, capacity building, fintech innovation, and knowledge dissemination



Fatawa Al-Ijarah wa Al-Ijarah al-Muntahiyah bi al-Tamlik (Arabic)

This volume explains key Islamic financial fatawa on leasing, providing a structured comparison of the International Islamic Fiqh Academy's resolutions with other institutions'.



Kazakhstan Islamic Finance Country Report

This report provides an in-depth analysis of the Islamic finance landscape in Kazakhstan, highlighting key developments, opportunities, and challenges within the region.



Catalyzing Social Entrepreneurship through Islamic Finance

This report explores how Islamic finance can support social entrepreneurship, offering policy recommendations to create robust frameworks for driving social impact in OIC countries.



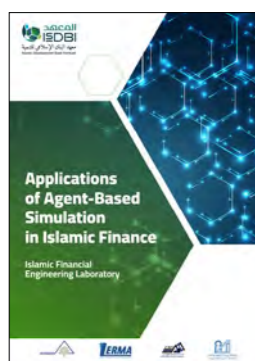
IsDBI-OPHI Briefs: Exploring Multidimensional Poverty Across IsDB Member Countries Using the Global MPI

This report assesses multidimensional poverty in IsDB member countries, offering policy-driven solutions to tackle poverty through evidence-based interventions and address emerging challenges like the climate crisis.



Artificial Intelligence and Islamic Finance: A Catalyst Financial Inclusion

This report explores how AI can enhance financial inclusion in Islamic finance, presenting a comprehensive framework to support micro-enterprises and offering policy solutions for sustainable development.



Applications of Agent-Based Simulation in Islamic Finance

This book explores the use of agent-based simulation to model complex systems in Islamic finance, addressing Shariah-compliant product design and fintech innovation for financial inclusion.



Insuring a Sustainable Future: Building Climate Resilience Through Takāful

This report examines the role of Takāful in building financial resilience for vulnerable Muslim communities, highlighting innovative strategies for climate risk mitigation through publicprivate partnerships.



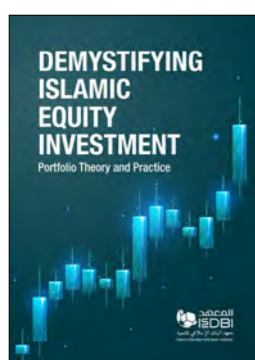
Heavy Tails and Coherent Risk Measures in Islamic Finance

This book introduces advanced econometric methods for Islamic finance, focusing on heavy tail distributions and coherent risk measures, offering practical insights for academics and industry professionals.



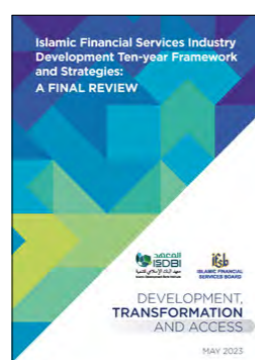
Bridging Islamic Finance Sustainability through Fintech

This report explores how fintech can enhance Islamic finance's contribution to sustainable development, with a focus on integrating social, economic, environmental goals into business models.



Demystifying Islamic Equity Investment


This book explores Shari'ah-compliant investing, providing insights into ethical portfolio strategies and the application of Islamic principles in financial decision-making.




Islamic Financial Services Industry Development Ten-Year Framework and Strategies: A Final Review

This report assesses the progress of the Islamic Financial Services Industry over the past decade, focusing on its expansion, regulatory improvements, and future adaptations.


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