

Implementation of Islamic Monetary Policy in Muslim-Majority Countries

Nurul Sakila¹, Rahayu Ningsih², Muhammad Furqon³, Viona Rosa⁴

¹²³⁴STAI-YDI Lubuk Sikaping Pasaman, Sumatera Barat, Indonesia

✉ sakilanurul907@gmail.com *

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Abstract

Central banks or authorized institutions establish monetary policy to maintain currency stability and control the money supply, which is the primary focus of macroeconomic stability. Currently, both conventional and Sharia economic systems influence monetary policy globally. Although Muslim-majority countries strive to implement sharia principles in domestic transactions, they must still adopt conventional monetary policies to adapt to international transactions. This article aims to examine the implementation of Islamic monetary policy in Muslim-majority countries. This research uses a literature review method that focuses on collecting and analyzing existing literature. The results show that Muslim-majority countries such as Malaysia, Indonesia, and countries in the Middle East have made significant efforts to integrate sharia principles into their monetary systems. This development is driven by the growing awareness of the Muslim community regarding the need for financial services that align with religious values. Sharia financial instruments such as sukuk, mudharabah, and murabahah are increasingly used as alternatives to conventional *riba* (interest)-based instruments. However, this implementation faces various challenges, including a lack of understanding and in-depth socialization of Sharia economic principles among the public and policymakers. Other challenges include the development of innovative and liquid Islamic monetary instruments to compete with conventional instruments, harmonization of regulations and supervision between Islamic and conventional institutions, and limited human resources with dual expertise. Continuous collaboration is needed to achieve a fairer and more sustainable financial system.

INTRODUCTION

A central bank or authorized institution issues monetary policy with the primary goal of maintaining and stabilizing the value of the currency for the sake of the stability and resilience of the country's economy. This policy also serves as a regulatory tool for financial institutions in setting interest rates and controlling the money supply to manage inflation.

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With monetary regulations, it is hoped that macroeconomic stability, the primary objective of this policy, can be achieved. (Idris, 2022). The implementation of Islamic monetary policy in Muslim-majority countries is an interesting and evolving topic in modern economics. Countries with significant Muslim populations are increasingly interested in integrating Sharia principles into their monetary policy frameworks. The primary goal of this implementation is to achieve economic stability and sustainable growth in accordance with Islamic teachings, which prohibit *riba* (interest), *gharar* (speculative uncertainty), and *maisir* (gambling).

This implementation process involves the development of Sharia-compliant monetary instruments and mechanisms, such as *sukuk* (Islamic bonds), *mudharabah* (profit-sharing), and *murabahah* (buying and selling with an agreed profit margin). Challenges in implementing Islamic monetary policy include developing liquid and efficient Islamic financial markets, harmonizing regulations across countries, and developing human resources skilled in Islamic economics and finance. A study by Khan (2010) in "Islamic Finance and Economic Development" highlights the importance of a robust regulatory framework and the development of innovative financial instruments for the successful implementation of Islamic monetary policy.

METHODS

The method I used was a literature review, a method often used and applied as a scientific method by a group of researchers. This method is part of library research that focuses on collecting and analyzing existing literature (Ayu, 2021). Research Method: The literature review method is a scientific method commonly used by researchers. The focus of this method is on collecting and analyzing existing literature.

i) Topic Analysis: This article specifically discusses distributive justice as a pillar of Islamic economic stability, ii) Application analysis: Analysis conducted based on a literature review shows that Muslim-majority countries such as Malaysia, Indonesia, and countries in the Middle East have attempted to integrate sharia principles into their monetary systems, iii) Instruments Used: Sharia financial instruments such as *sukuk* (sharia bonds), *mudharabah* (profit sharing), and *murabahah* (buying and selling with an agreed profit margin) are increasingly being used as alternatives to conventional interest-based or usury-based instruments, iv) Challenges analysis: Lack of Understanding: One of the main challenges faced is the lack of in-depth understanding of sharia economic principles among the public and policy makers, Instrument Development: The development of innovative and liquid sharia monetary

instruments still requires greater efforts to be able to compete with conventional instruments, Regulation harmonization: Differences in accounting standards, sharia interpretations, and dispute resolution mechanisms can hinder the integration of sharia financial markets, Limited Human Resources: Limited human resources who are experts in conventional and sharia economics are also an obstacle.

RESULT AND DISCUSSION

The implementation of Islamic monetary policy in Muslim-majority countries has shown significant progress but also faces various complex challenges. Studies show that countries such as Malaysia, Indonesia, and those in the Middle East have made various efforts to integrate Sharia principles into their monetary systems. Sharia financial instruments such as sukuk, mudharabah, and murabahah are increasingly being used as alternatives to conventional interest-based instruments (riba). This development is driven by the growing awareness of the Muslim community regarding the need for financial products and services that align with their religious beliefs.

However, the implementation of Islamic monetary policy also faces several challenges. One major challenge is the lack of in-depth understanding and dissemination of Islamic economic principles among the wider public and policymakers. This often leads to hesitation and resistance to the adoption of the Islamic financial system. Furthermore, the development of innovative and liquid Islamic monetary instruments still requires greater efforts to compete with conventional instruments. Another challenge relates to the harmonization of regulations and supervision between Islamic and conventional financial institutions, both at the national and international levels. Differences in accounting standards, sharia interpretations, and dispute resolution mechanisms can hinder the integration and efficiency of Islamic financial markets (Hudaib, 2019). Furthermore, the limited human resources with dual expertise in conventional and sharia economics also hinder the development of the Islamic financial industry as a whole.

Case studies in several Muslim-majority countries provide a diverse picture of the implementation of Islamic monetary policy. Malaysia, for example, has demonstrated significant progress in developing a comprehensive Islamic financial ecosystem, including a vibrant sukuk market and various Sharia-compliant investment instruments (Financial Services Authority, 2022). Meanwhile, Indonesia, the world's most populous Muslim country, continues to strive to strengthen Islamic financial regulations and infrastructure to contribute more significantly to the national economy.

Overall, the results and discussions regarding the implementation of Islamic monetary policy in Muslim-majority countries demonstrate significant potential for creating a fairer, more stable, and more sustainable financial system. However, realizing this potential requires sustained efforts to improve understanding, develop innovative instruments, strengthen regulations, and enhance human resource capacity in the Islamic financial sector (Sobarna, 2019). Collaboration between governments, central banks, Islamic financial institutions, academics, and the wider community is key to the successful implementation of Islamic monetary policy in the future.

The implementation of Islamic monetary policy in Muslim-majority countries has shown significant progress but also faces various complex challenges. This literature review provides an overview of integration efforts, the instruments used, and the challenges involved.

Islamic Monetary Policy

Monetary policy in Islam is fundamentally different from conventional because its goal is not only price stability, but also achieving economic welfare (*falah*) and distributive justice in accordance with Sharia principles.

Basic Points	Islamic Economics	Conventional Economy
The main purpose	Stability and Distribution Justice (achieving <i>falah</i>).	Price stability and economic growth (through inflation control).
Key Instruments	Profit sharing (<i>Profit and loss sharing</i>) like <i>Mudharabah</i> and <i>Musyarakah</i> , sukuk, and zakat.	Interest rates (discount rates), open market operations (buying and selling securities), and minimum reserve requirements.
Core Prohibition	Riba (interest), gharar (uncertainty), and Maysir (gambling).	There is no specific prohibition on interest, making it a primary instrument of policy.

The research background states that although Muslim-majority countries aspire to implement Sharia, they remain influenced by conventional systems in international transactions. This creates a dualistic challenge: Central banks must stabilize the economy using Sharia-compliant (*riba*-free) instruments domestically while still interacting with the

global market dominated by interest rates. The Sharia theoretical framework, which focuses on distributive justice (falah), demands different and more innovative instruments than simply controlling the money supply through interest rates, which has been the primary focus of conventional policy.

Implementation and Development of Sharia Monetary Instruments

Muslim-majority countries have demonstrated concrete efforts to integrate Sharia principles into their monetary systems. i) Integration of Sharia Principles: Countries such as Malaysia, Indonesia, and countries in the Middle East have pioneered this effort. The main impetus is the increasing awareness of the Muslim community regarding the need for products and services that are in accordance with religious values. ii) Use of Alternative Instruments: Sharia financial instruments such as sukuk (Sharia bonds), mudharabah (profit sharing), and murabahah (sale and purchase with a profit margin) are increasingly being used as alternatives to conventional interest-based or *riba*-based instruments. For example, Malaysia has succeeded in developing a comprehensive Sharia financial ecosystem and an active sukuk market. iii) Indonesia's role: Indonesia, as the country with the largest Muslim population, continues to strive to strengthen its Sharia financial regulations and infrastructure to increase its contribution to the national economy.

Complex Challenges in Implementation

Despite progress, the implementation of Islamic monetary policy faces a number of complex challenges: Lack of Understanding and Socialization: There is still a lack of in-depth understanding of the principles of Islamic economics among the general public and even policymakers. This often gives rise to doubts and resistance to the adoption of the Islamic financial system. Instrument Development: Greater efforts are needed to develop innovative and liquid Islamic monetary instruments to be able to compete effectively with established conventional instruments. This challenge is also highlighted by Khan (2010) who emphasizes the need for the development of innovative financial instruments.

Regulatory Harmonization: Harmonization of regulations and supervision between Islamic and conventional financial institutions is needed, both nationally and internationally. Differences in accounting standards, Sharia interpretations, and dispute resolution mechanisms can hinder market integration and efficiency. Limited Human Resources (HR): The limited availability of human resources with dual expertise in conventional economics and Sharia principles is an obstacle to the comprehensive development of the Islamic financial industry.

Overall, the implementation of Islamic monetary policy has great potential to create a fairer, more stable, and more sustainable financial system. However, achieving this requires sustained efforts and close collaboration between governments, central banks, Islamic financial institutions, academics, and the wider community.

CONCLUSION

This study concludes that the implementation of Islamic monetary policy in Muslim-majority countries like Malaysia and Indonesia has shown encouraging progress. This development is characterized by these countries' active efforts to integrate Sharia principles into their monetary frameworks. The primary driver behind this trend is the growing awareness among Muslims of the need for financial services that align with religious values.

However, there are crucial challenges that need to be addressed to realize a fairer and more sustainable financial system, namely: i) lack of understanding and socialization of Sharia economic principles in society and policy makers, the need to develop innovative and liquid Sharia monetary instruments to be able to compete with conventional instruments, ii) Harmonization of regulations and supervision between Sharia and conventional institutions, iii) the need to develop innovative and liquid Sharia monetary instruments to be able to compete with conventional instruments, iv) limited human resources who have dual expertise in conventional and Sharia economics.

The success of future implementation depends on continued efforts to address these challenges through close collaboration among all relevant parties.

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