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The Dynamics of Islamic Finance in Kazakhstan: Exploring Opportunities and Addressing Challenges

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ABSTRACT

Introduction: *This paper explores the burgeoning field of Islamic finance in Kazakhstan, highlighting the opportunities and challenges that lie ahead. Islamic finance, which adheres to Sharia law, provides a distinct alternative to conventional banking systems. As Kazakhstan seeks to diversify its financial sector and attract investments from Muslim-majority countries, understanding the dynamics of Islamic finance becomes crucial. This study examines the legislative framework, market potential, key players, and the socio-economic implications of Islamic finance in Kazakhstan. The case study of existing Islamic banks is given, and their financial performance is examined.*

Methods: *This research employed a qualitative approach, incorporating a literature review and descriptive-exploratory analysis. Primary data were obtained from academic literature, official reports from international financial institutions, Kazakh government regulations, and publications related to the development of Islamic finance in Central Asia. Data analysis techniques included reduction, categorization, and thematic interpretation to identify the dynamics, opportunities, and challenges associated with the implementation of Islamic finance in Kazakhstan. This approach was chosen to provide an in-depth understanding of the actual conditions and prospects of Islamic finance, while also generating strategic recommendations for the development of the industry at the national and regional levels.*

Results: *The research paper also highlights the obstacles faced by the Islamic finance sector and the potential for expanding its implementation.*

***Conclusion and suggestion**: The paper further recommends solutions for integrating Islamic finance into Kazakhstan's economy.*

***Keywords:** Economic Development, Financial Diversification, Islamic Bank, Islamic Finance*

Paper type: Research paper

INTRODUCTION

Islamic finance is a financial system that operates in accordance with Islamic law, known as *Shariah*, which prohibits interest *(riba)*, excessive uncertainty *(gharar)*, and investment in unethical or prohibited activities (haram). Instead of conventional interest-based transactions, Islamic finance relies on principles of profit-sharing, risk-sharing, and asset-backed financing. Key financial instruments include *Murabaha* (cost-plus financing), *Mudarabah* (profit-sharing partnership), *Musharakah* (joint venture), *Ijara* (leasing), and *Sukuk* (Islamic bonds). These mechanisms ensure ethical, transparent, and socially responsible financial practices (Shah, 2015; Shah *et al.,* 2018; Siddique, 2017).

Islamic finance has gained global recognition as a stable and resilient alternative to conventional finance, particularly in times of economic crises. It promotes financial inclusion by providing *Shariah*-compliant solutions to Muslim populations and ethical investors worldwide. Countries such as Malaysia, Saudi Arabia, the UAE, and the UK have established strong Islamic finance sectors, while others, including Kazakhstan and various Central Asian nations, are actively working to develop this industry. The Islamic financial system is expanding beyond traditional Muslim-majority markets, attracting interest from non-Muslim investors due to its principles of fairness, ethical investment, and risk-sharing. As it continues to grow, Shah et al., (2021) have documented that Islamic finance plays a crucial role in fostering sustainable economic development and enhancing global financial stability. Kazakhstan's cultural alignment with the principles of Islamic finance reinforces this trend, as the concept resonates well with the ethical and risk-sharing foundations of the system. According to data from the Statistics Agency, approximately 70% of Kazakhstan's population identifies as Muslim, indicating a significant potential market for Islamic financial services.

Additionally, as the largest economy in Central Asia, Kazakhstan is proactively working to diversify its financial sector and reduce its dependence on conventional banking systems. The principles of Islamic finance, which emphasize ethical investment, shared risk, and prohibition of interest *(riba)*, offer a viable and attractive alternative that aligns with the country's broader financial inclusion and economic diversification goals. Sharpe (1995) has explored the importance of government support in giving investors confidence in any field. We observe that the government has also taken steps to introduce legislative and regulatory frameworks that support the integration and growth of Islamic finance institutions, thereby facilitating a more conducive environment for its development.

This paper explores the global expansion of the Islamic finance industry and its promotion within Central Asian economies, with a particular focus on Kazakhstan. It aims to provide an in-depth analysis of the opportunities and challenges associated with the establishment and growth of Islamic finance in the country. Furthermore, case studies of two Islamic banks operating in Kazakhstan are examined to highlight both the hurdles faced and the prospects available within the industry. Based on these insights, the paper concludes with a set of recommendations and strategic suggestions for the effective integration of Islamic finance into Kazakhstan's broader financial and economic landscape.

Islamic finance has emerged as one of the fastest-growing segments of the global financial industry, offering ethical and Shariah-compliant alternatives to conventional finance. With assets surpassing trillions of US dollars globally, Islamic finance is increasingly recognized as a sustainable and resilient model that emphasizes risk-sharing, asset-backed financing, and prohibition of interest (*riba*). While the industry has seen rapid growth in regions such as the Middle East and Southeast Asia, its development in Central Asia remains relatively nascent yet promising (Ponziani & Mariyanti, 2020). Kazakhstan, as the largest economy in Central Asia, occupies a strategic position in advancing Islamic finance within the region. The country has shown an increasing interest in diversifying its financial sector, reducing its dependency on conventional banking, and exploring alternative mechanisms that align with both international best practices and the cultural and religious preferences of its population. Although Muslims constitute a majority in Kazakhstan, the penetration of Islamic financial products remains limited compared to conventional finance. This creates both opportunities and challenges for the sector's expansion (Ibrahim Atah et al., 2018).

From an opportunity perspective, Kazakhstan has several enabling factors that could facilitate the growth of Islamic finance. First, the government has demonstrated political will by introducing legal reforms and establishing regulatory frameworks that recognize Islamic banking, *sukuk issuance*, and *takaful* (Islamic insurance). Second, Kazakhstan's aspiration to become a financial hub through initiatives such as the *Astana International Financial Centre (AIFC)* provides a strong institutional foundation for attracting international investors and Islamic financial institutions. Third, the country's growing infrastructure and energy needs present significant avenues for Islamic finance instruments, such as *sukuk*, to fund sustainable development projects (Alshater et al., 2022). At the same time, several challenges hinder the effective integration of Islamic finance into Kazakhstan's financial ecosystem. These include limited public awareness of Islamic financial principles, insufficient human capital and expertise in *Shariah*-compliant finance, and the dominance of conventional banks, which remain the primary source of financial intermediation. Moreover, the regulatory environment, although improving, still faces gaps in ensuring full *Shariah* compliance, investor protection, and integration with global Islamic financial markets (Widarjono et al., 2022).

Another crucial aspect is the cultural and socio-religious context**.** While Kazakhstan is a Muslim-majority country, levels of religious practice and awareness of Islamic economic principles vary significantly across the population As a result, demand for Islamic financial products has not yet fully developed, necessitating targeted educational campaigns and awareness initiatives to establish trust and attract clients. The dynamics of Islamic finance in Kazakhstan thus reflect a dual reality: on the one hand, significant potential for growth supported by government initiatives and strategic geographic positioning; on the other hand, practical constraints that require comprehensive strategies to overcome. Exploring these dynamics in detail is crucial for identifying pathways to strengthen the Islamic finance ecosystem in Kazakhstan, positioning it as a regional leader in Shariah-compliant financial services, and ensuring its contribution to sustainable economic development (Budi & Faizin, 2024).

LITERATURE REVIEW

Global Landscape of Islamic Finance

The Islamic finance industry has been growing significantly in the global arena, reaching assets of approximately $4.5 trillion in 2022. (ICD -LSEG Islamic Finance Development Report, 2023) The main hubs of Islamic finance worldwide are the Gulf Cooperation Council countries, Iran, Malaysia, Pakistan, and Muslim-majority countries such as those in Central Asia, as well as European countries seeking to attract investments in line with Islamic finance principles (Shah *et al.,* 2018). Over the past decade, the Islamic finance sector has evolved from a specialized market into a global business in several countries, demonstrating how a small sector can grow into a substantial independent industry. This growth has been supported by strong balance sheets, significant profits, a favorable regulatory framework, and sustained demand from both investors and customers worldwide. The assets of Islamic finance are estimated to increase, reaching US$6.7 trillion globally by 2027. This projection is highlighted by the following factors: where GCC, Malaysia, Indonesia, and other Muslim majority markets have been improving their own Islamic finance industry, and Pakistan's attempts to convert its financial system into an Islamic Riba-free status. In other parts of the world, such as West Africa, regulatory bodies are seeking to implement Islamic financial products through laws. (Shaima Hasan & Shereen Mohamed, 2024).

In Diagram 1, the growth of Islamic Finance Assets is shown from 2016 to 2022, according to the results derived from the report, which was developed in cooperation with the Islamic Corporation for the Development of the Private Sector (ICD) of the Islamic Development Bank Group. The report analyzes statistics from 136 countries worldwide across five indicators, including financial performance, governance, knowledge, sustainability, and awareness.

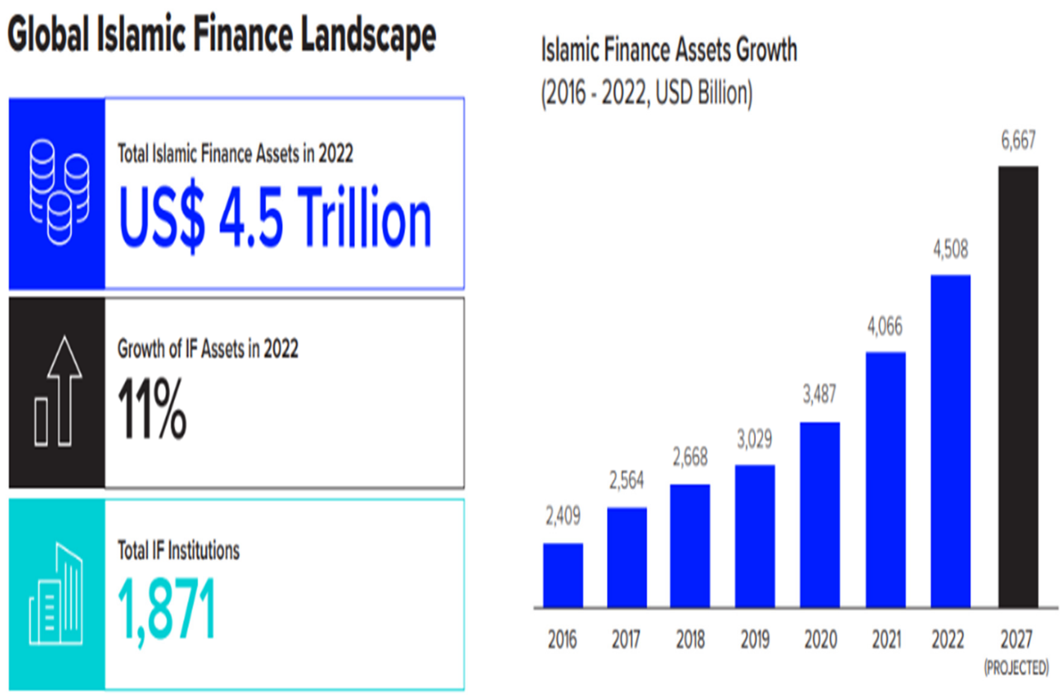


Figure 1. Islamic Finance Assets Growth, 2016-2022
Source: ICD -LSEG Islamic Finance Development Report, 2023

In Figure 1, the Gulf countries are recognized as the region with the most advanced Islamic finance development, with 66% assets held by Islamic financial institutions. Iran, Pakistan, and other countries are becoming increasingly aligned with Islamic finance principles, where all banks and financial institutions are required to adhere to strict Islamic regulations. Countries such as Malaysia, Indonesia, Turkey, and the UAE operate under a mixed economic system, where both traditional and Islamic financial systems coexist (Mohamed Damak et al., 2023).

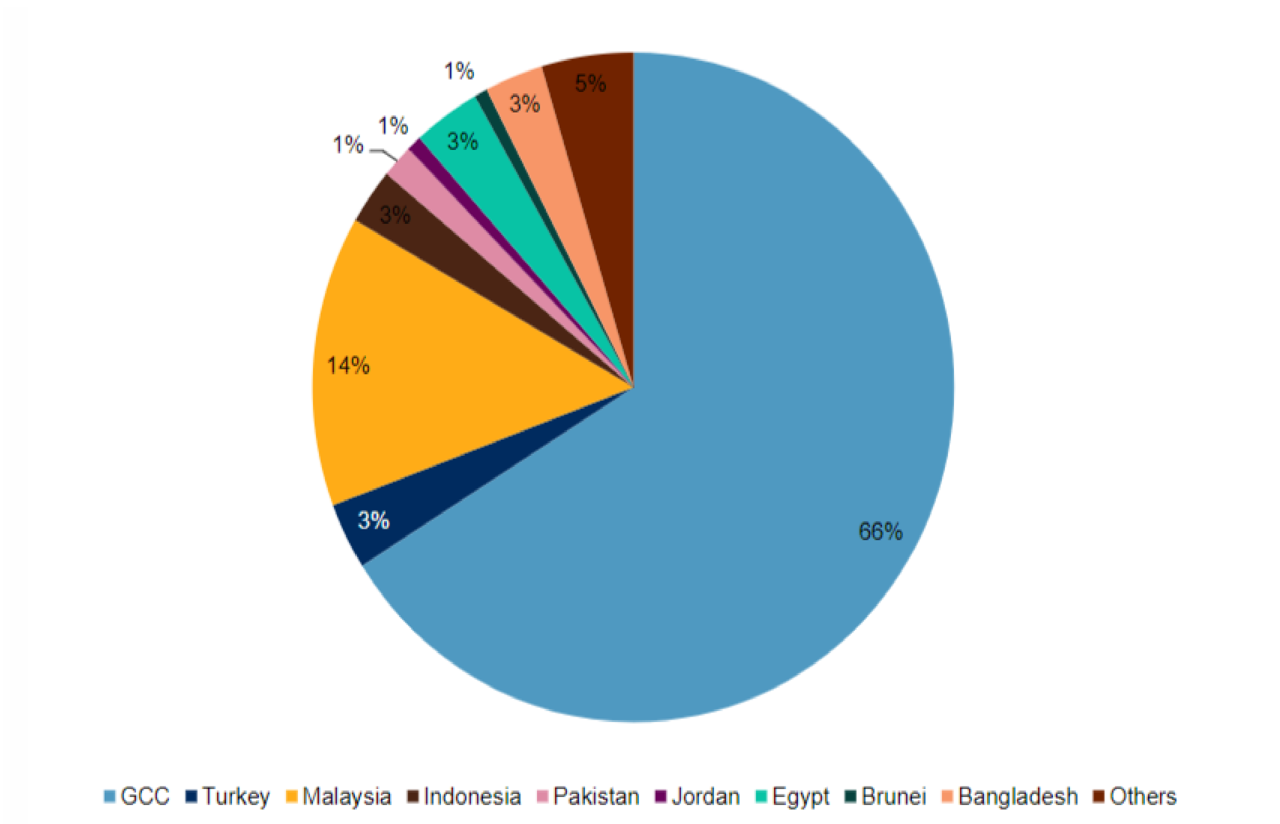


Diagram 1. Assets of Islamic finance by countries
Source: Central Banks, S&P Global Ratings.

Almost a quarter of the global Islamic finance market is located in the Asia-Pacific region. *Shariah*-compliant institutions account for nearly 14% of Malaysia's financial sector. Kuala Lumpur plays a significant role in advancing the global *sukuk* market and helps set international standards through the Islamic financial services board. Following the 2008 global financial crisis, Islamic finance emerged as a stable alternative to the Western banking system, which was faltering at the time. *Sukuk* offered a promising path for entering new markets, Islamic funds created opportunities for substantial liquidity, and Islamic banking provided a means to capitalize on the local Muslim population. London has since become the center of Islamic finance in the Western world. Today, the UK has five licensed Islamic banks, while over twenty conventional banks offer Islamic finance products. Luxembourg is home to around thirty Islamic funds and became the first Eurozone country to issue sovereign *sukuk*. In France, with its largest Muslim population in Europe, French investment banks offer *Shariah*-compliant products to meet the demands of its international clientele.

The African market, characterized by vast territories, limited financial education, and a lack of regulatory frameworks, presents challenges for Islamic banks. If *Shariah*-compliant finance is to grow in Africa, it is likely to be driven by banks from Egypt, Sudan, and Morocco. In Africa, Islamic finance typically expands through private or sovereign *sukuk*, rather than banking. African governments view Islamic finance as a way to attract foreign investment from the international market, but outcomes have been modest so far (Domat, 2024).

METHOD

This study employed a qualitative, descriptive, and exploratory approach. This approach was chosen to gain an in-depth understanding of the dynamics, opportunities, and challenges associated with the development of Islamic finance in Kazakhstan. The research was designed as a library-based study (desk research) supported by secondary data from international reports, government regulations, and scholarly publications. Primary data from government regulations, official policy documents, and reports from Islamic financial authorities in Kazakhstan. Secondary data journal articles, academic books, international research reports (e.g., IMF, IFSB, IDB), and credible media coverage. Data were collected through a literature review of international journals, books, and policy reports. Online data retrievaled from reliable institutional sources. Document analysis of regulations and financial reports related to Islamic finance in Kazakhstan. The study employed thematic analysis, which involves data reduction, selection, and extraction of relevant information on dynamics, opportunities, and challenges. Categorization: classifying data into themes such as regulation, products, infrastructure, and socio-economic challenges. Interpretation: drawing descriptive conclusions about the dynamics of Islamic finance in Kazakhstan and providing strategic recommendations. Data validity was ensured through source triangulation, which involved cross-checking information from multiple documents, reports, and publications to confirm the accuracy and consistency of findings.

Research Design

Islamic Finance in Central Asia

The Islamic Development Bank (IsDB) has played a crucial role in promoting financial projects in the region that align with Islamic principles. Kyrgyzstan became a member of the IsDB in 1993, followed by Turkmenistan in 1994, Kazakhstan in 1995, Tajikistan in 1996, and Uzbekistan in 2001. In 2018, the IsDB established its regional hub for Central Asia in Kazakhstan. By 2022, the IsDB had funded 378 projects in the region, with a total investment of $6.88 billion. Islamic finance in Central Asia is relatively nascent, with Kazakhstan leading the establishment of a regulatory framework and attracting Islamic financial institutions. Kazakhstan is the first country in the CIS region to implement a legislative framework for the development of Islamic finance.

Table 1. The Dynamics of Islamic Finance development in Kazakhstan

Dates	Major achievements
2009	Kazakhstan became first nation in CIS region to create a legal framework supporting Islamic finance, making amendments to its Banking and banking activities law.
2010	• Al Hilal Islamic Bank, a fully owned subsidiary of the Abu Dhabi Investment Council, launched as a full-service Islamic bank under Kazakhstan-UAE intergovernmental agreement. • MIS Takaful emerged as a Kazakhstan's first Islamic insurance provider.
2011	• Government authorized the Roadmap for Islamic Finance Development until 2020, outlining Islamic securities issuers, investors and market participants, aiming to support new Islamic banks and provide stable conditions for the sector's growth. • A member Country Partnership Strategy (2012-2014) was signed between Kazakhstan and Islamic Development Bank. • The Development Bank of Kazakhstan issued the first Sukuk denominated in Malaysian Ringgit, valued at $76.7 million • Kazakhstan's National Bank joined the Islamic Financial Services Board (IFSB).

2013	• The Islamic Corpration for Development of the Private Sector (ICD) acquired shares in Zaman Bank, which later became Kazakhstan's first retail bank. • ICD, along with local and international investors, launched the first Kazakhstani Ijara company JSC.
2014	• The Global Islamic Finance Award (GIFA) was awarded to Kazakhstan's first president Nursultan Nazarbayev • The National Bank of Kazakhstan joined the AAOIFI and the IIFM.
2015	• Kazakhstan developed legal frameworks for Islamic banking, Islamic insurance, and leasing. Takaful was recognized as a unique form of insurance. • Legal frameworks were introduced to allow conversion of conventional banks to Islamic banking.
2017	• Zaman Bank completed its conversion into Islamic Bank, receiving a license from the National Bank of Kazakhstan. • Al Hilal Islamic Bank introduced retail banking products
2018	• Astana International Finance Center is officialy opened in 5 July 2018 year, with Islamic finance as a core focus. • AAOIFI established an exam center at the AIFC • AIFC Advisory council on Islamic Finance was created.
2019	• In collaboration with Qatar's Hamad Bin Khalifa University, AIFC established an Islamic Finance Center at Al Farabi Kazakh National University. • the AIFC Central Shariah Advisory Board was formed • A partnership between INCEIF and AIFC was intitated.
2020	• The Qatar International Islamic Bank's Sukuk was addeed to the official list of the Astana International Exchange (AIX), totalling $500 million • Agreements were reached with Kazakhstan Ijara Company Limited fpr $3billion tenge ($7 million) and Al Hilal Bank for 10 billion tenge ($24 million) using murabaha and ijara products. • AIFC lunched Masterplan of Islamic Finance for Republic of Kazakhstan 2020-2025 developed by ZicoShariah company financed by IsDB.
2022	• The AIX cross-listed three sukuk issued by the Islamic Development Bank, with terms of five years and denominations of 1 billion euros for Green Sukuk, $1.5 billion for SustainabilitySukuk, and $2billion for Traditional Sukuk. • AIX launched its first Shariah-compliant Exchange-Traded Notes, called iX Islamic ETNs.
2023	Organization of international business forum «Business and Islam: Issues of finance and investments» at Nur Mubarak Egyptian university by special invitation of well-known Professor of Islamic Economics, Monzer Kahf.
2024	Islamic Finance Country Report for Kazakhstan launched at Astana Finance Days in collaboration between IsDB, AIFC, and CSQ Law.

Sources: NBK, Salikhova, AIFC, (2016)

Uzbekistan is actively working to attract Islamic financing by negotiating bilateral agreements with Islamic financial institutions and introducing Islamic windows in existing commercial banks. The Islamic cooperation for the development of the private sector has partnered with several banks, including Bank Ipak Yuli, Alokabank, Trustbank, Invest Finance Bank, KapitalBank, Asakabank, Turonbank, Uzpromstroybank, KhamkorBank, and Asia Alliance Bank to promote the growth of Islamic Finance. Most of the funding is provided through guarantees based on *Murabaha* financing. At the same time, businesses such as

Uzum Nasiya, Alif Nasiya, and Iman Invest have started operating in line with Islamic principles. Currently, Uzbekistan is considering its capital, Tashkent, to be financial center of Central Asia, establishing a special free economic zone, International Finance Center Tashkent. According to research made by experts, the establishment of the International Finance center in Tashkent will provide long-term sustainable investment growth, increasing counntry's GDP by 1 % yearly, and attracting investment in the amount of 7-8 billion by 2028.

The Islamic banking law in Tajikistan took effect on August 5, 2014. Tawhidbonk is a Joint-Stock Company and is the first fully operational Islamic bank in the country. The transition of Sohibhorbonk into a full-fledged Islamic bank began in October 2017. Tawhidbonk received its banking license in September 2019. The development of Islamic finance in the Kyrgyz Republic began in 2006 with the launch of a pilot project by Eco Islamic Bank, supported by the Islamic Development Bank. In 2009, amendments were made to the laws on « Banks and Banking in the Kyrgyz Republic » and « The National Bank of the Kyrgyz Republic» to integrate Islamic banking concepts. Despite its early stage of development, the country's Islamic finance sector comprises one bank and three microfinance companies that operate entirely in accordance with Islamic finance principles. Additionally, the non-profit « Association of Islamic Economics, Finance, and Industry Development» plays a key role in supporting new market participants, offering advisory services to conventional financial institutions, and providing training on Islamic finance. The Muslim countries of Central Asia have demonstrated themselves to be excellent prospects for the development of Islamic banking and finance for over a decade. Despite the challenges faced, CIS countries showed relative success in advancing Islamic finance and banking initiatives.

Opportunities and Challenges in Kazakhstan

In the case of Kazakhstan, we have opportunities to capitalize on, along with challenges to overcome, for the sake of Islamic finance growth. Kazakhstan has introduced regulatory support to facilitate Islamic banking and finance, including the establishment of the Astana International Financial Centre (AIFC). To witness the growth of Islamic finance, the study shows that the new regulatory frameworks and institutions must be developed to strengthen Kazakhstan's financial infrastructure. Islamic finance departments at current regulatory bodies, such as the National Bank of Kazakhstan and the Agency of the Republic of Kazakhstan for the Regulation and Development of the Financial Market, must be established. The competitiveness of the AIFC (Astana International Finance Center) lies in its ability to utilize Islamic financial business structures, such as Islamic wealth, asset, and fund management, Islamic banking, and Islamic windows, to attract international players to open and register their regional operations on the AIFC platform. AIFC could capitalize on the growing interest in the Islamic finance industry among regulatory authorities and other market players in neighboring countries, such as Uzbekistan, Tajikistan, Azerbaijan, and Kyrgyzstan, to attract significant Islamic business to its platform.

With a significant Muslim population and increasing demand for ethical finance, Kazakhstan presents a promising market for Islamic financial products. According to the United Nations' estimates, the current population of Central Asia is approximately 82 million people. It means Kazakhstan has enormous potential to become the regional hub of Islamic finance in Central Asian countries by offering unique solutions in *Shariah*-compliant services and further attract Muslim countries' foreign investment into this market. Economic diversification**,** Islamic finance can contribute to Kazakhstan's goal of diversifying its economy from oil dependency. Islamic finance offers *Shariah*-compliant financial products, providing an alternative to conventional financial products. This diversification can attract a wide range of customers, muslims and non-muslims, including those who prefer *Shariah*-compliant options. Foreign investment**,** attracting investments from Muslim-majority countries and global investors interested in ethical finance, can bolster economic growth and financial stability. Kazakhstan presents an excellent opportunity to become the hub of Islamic finance in Central Asia, thanks to its strategic location at the heart of the Eurasian continent. Economic growth and stability, the inclusion of Islamic finance into Kazakhstan's economy can positively contribute to its economic growth and financial stability. Islamic finance promotes a risk-sharing philosophy and prohibits excessive speculation and uncertainty, thereby fostering a more stable financial system. To capitalize on these opportunities, Kazakhstan will continue to enhance its regulatory environment, raise awareness of Islamic finance among the population, and foster expertise in Islamic finance. Training professionals in *Shariah*-compliant finance and developing a legal framework must be included in further plans for Islamic finance development in the near future.

Challenges

There is a significant need to increase awareness and understanding of Islamic finance among both consumers and financial professionals. The development of Islamic finance often requires educational programs and initiatives to inform financial professionals and the general public about the principles and advantages of Islamic finance. One of the key findings of this research, based on a survey conducted in Kazakhstan, revealed a deficient level of knowledge about Islamic banking products and services among the population, despite a high level of interest in these products and services. In response, efforts should be made to educate the public through targeted marketing campaigns, media outreach, and the organization of conferences, workshops, and seminars. These initiatives are essential due to the widespread lack of understanding regarding the philosophy and nature of Islamic banking and finance among the general public and those working within the industry. The research also concluded that religious beliefs are the primary factor for customers when choosing an Islamic bank; in contrast, other considerations such as service quality, pricing, and a bank's reputation are also important. Islamic bankers should not overlook these factors.

Expertise and knowledgeable staff are currently available in Kazakhstan; however, there is a significant shortage of trained, skilled, and professional staff in the Islamic finance sector. It is not possible to sustain the growth and credibility of Islamic banks without focusing on the very special human resource requirements of the industry. That is why the education and training specialists in Islamic finance must be executed at local universities in collaboration with foreign institutions. Regulatory harmonization, aligning Kazakhstan's regulatory framework with global standards while ensuring Shariah compliance, presents significant challenges. Countries seeking to develop Islamic finance must establish a regulatory system that incorporates *Shariah* principles. Kazakhstan may have already created, or is in the process of creating, such a framework to support Islamic financial activities.

A well-designed regulatory and policy structure is essential for fostering a comprehensive and efficient Islamic banking industry. Islamic banks must strive to ensure that their structures and products adhere to Shariah principles, which can encourage Muslim communities to adopt these alternative financing options. Additionally, these institutions can attract a wider audience by offering innovative products focused on risk management, mitigation, and additional options. It is reasonable to anticipate that certain Islamic banking products and services involve risks distinct from those in conventional banking. Therefore, prudential regulations must be established to address the unique risk characteristics of Islamic financial products. Enhancing the regulatory framework and aligning Islamic financial regulatory and supervisory standards with evolving international practices are essential for the growth and development of the Islamic banking sector. Achieving this goal will necessitate greater collaboration and oversight from domestic regulators, as well as international standard-setting bodies like the IFSB, AAOIFI, and other Islamic banking and financial institutions.

The legal framework remains the single most important determinant of a sound Islamic banking segment. The laws should specify the activities that various Islamic banks are permitted to undertake. Additionally, tax neutrality can significantly contribute to the growth of Islamic banks, yet tax regulations in Kazakhstan currently hinder the competitiveness of the Islamic banking sector. Al Hilal Bank, for instance, faces legislative and operational challenges, particularly in securing tax advantages for various banking products, such as commodity Murabaha, Ijara, and Wakala. To build confidence, stability, and a level playing field for Islamic financial institutions, existing laws should be reviewed and further revised.

Market infrastructure, including *Sharia*-compliant financial instruments and liquidity management tools, is essential for developing the necessary market infrastructure. The agriculture, mining, and construction sectors can raise Islamic bonds, known as *sukuk*, to finance their operations. Salam and Istisna - Islamic finance instruments must be developed in line with Sukuks for these sectors. Moreover, *Waqf* models can be applied to state-owned assets that are not functioning to determine their purposes for future use.

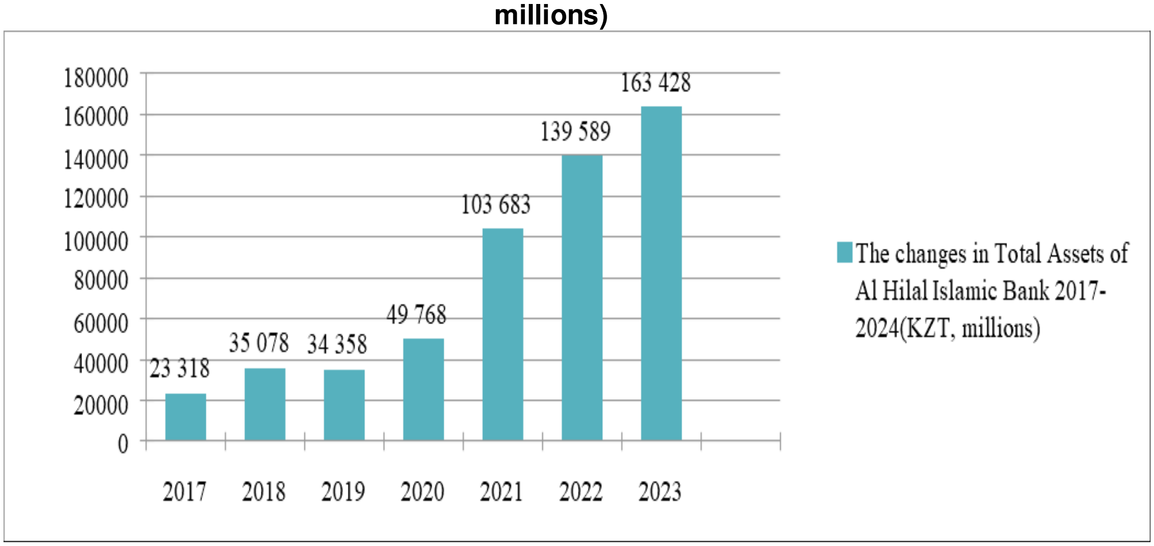
Competition with conventional banks, Islamic banks must compete with well-established traditional banks, which can be challenging given the nascent state of the market. Islamic banks operate under *Shariah* principles, which prohibit the payment or receipt of interest, unlike conventional banking. Instead, Islamic banks engage in profit-and-loss sharing arrangements. In Kazakhstan, Islamic banking institutions need to expand their range of products, catering not only to the Muslim population but also to non-Muslims. Additionally, Islamic banking products should be made accessible nationwide through the establishment of new branches. Islamic banks must also demonstrate transparency by openly sharing necessary information about their operations, policies, decision-making processes, and adherence to both regulations and Shariah law. This research has recommended steps to advance Islamic finance products through marketing efforts, securing approval to open Islamic banking windows within conventional banks, and integrating fintech into Islamic finance operations, despite the introduction of a comprehensive legal framework.

DISCUSSION

Al Hilal Bank

As one of the first Islamic banks in Kazakhstan, Al Hilal Bank's experiences offer valuable insights into the operational and regulatory challenges faced by Islamic financial institutions in the country. "Al Hilal Islamic Bank" is a subsidiary of the Abu Dhabi Commercial Bank Group (ADCB), which was established as the first Islamic bank in Kazakhstan and the CIS region in 2010, following an agreement between the governments of the UAE and Kazakhstan. From its opening, the bank has been offering solutions in accordance with Shariah principles, limited to corporate clients only. In 2017, Al Hilal Bank began offering Islamic banking products to private clients in Kazakhstan. Nowadays, banks provide products and services according to Shariah rules, ranging from accounts and deposits to cash services and treasuries through their branches in Astana, Almaty, and Shymkent. A significant rise in assets is recorded, from 23,318 billion KZT to 163,428 billion KZT, during the period from 2017 to 2023, as shown in Diagram 3.

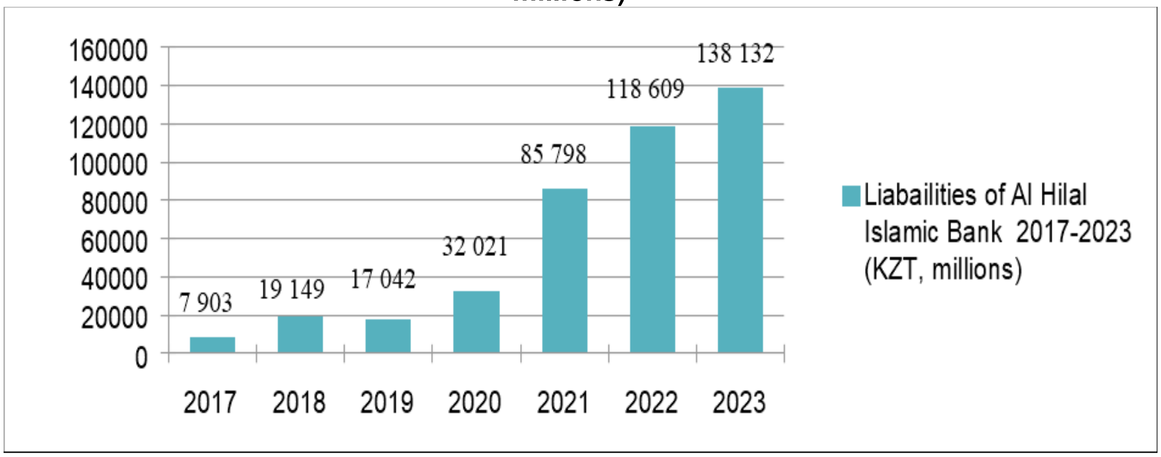
Diagram 2. The Total Assets of "Al Hilal Islamic Bank" through years 2017-2024 (*KZT, millions*)



Source: Compiled by author, Al Hilal Islamic Bank Audit reports

The growth of Liabilities is shown on Diagram 3, whereas it was recorded 85.798 billion KZT in 2021, and the amount had risen dramatically to 138,132 billion KZT in 2023. (Diagram 4)

Diagram 3. The Liabilities of al Hilal Islamic Bank through years 2017-2023 (KZT, millions)



Source: Compiled by author, Al Hilal Islamic Bank Audit reports

During the period Liquid Assets to Total Assets Ratio decreased from 54,3 percent to 17,6 percent respectively from 2017 to 2023 years as shown on Table1.

Table1. Liquidity Ratio

Liquidity Ratios							
Particulars	2017	2018	2019	2020	2021	2022	2023
Liquid Assets to Total Assets	54,3	70,9	48,8	49,4	20,5	6,6	17,6

Capital to Total Assets Ratio was 66,1 percent in 2017, then it was decresed till 15,5 percent in 2023 as shown in Table 2 below.

Table 2. Capital Ratio

Capital Ratio (%)							
Particulars	2017	2018	2019	2020	2021	2022	2023
Capital to Total Assets Ratio	66,1	45,4	50,4	35,7	17,2	15,0	15,5

ROE (Return on Equity) improved to 17,1 percent while ROA (Return on Assets) remained at 2,6 percent in 2023. (Table 3)

Table 3. Profitability Ratio

Profitability Ratios (%)							
Particulars	2017	2018	2019	2020	2021	2022	2023
ROE	5,3	3,5	8,0	2,4	0,8	14,8	17,1
ROA	3,5	1,6	4,0	0,9	0,3	2,2	2,6

Source: Compiled by author, 2025

Al Hilal Islamic Bank offers current accounts and investment accounts that operate in accordance with Islamic contracts. The Bank maintains deposit accounts for its individual clients, utilizing the Wakalah and Mudarabah investment concepts. For example, in the Wakalah deposit scheme, the client entrusts their funds to the bank, which invests them in a

Shariah-compliant project. The profit is then shared between the bank and the customer. In this concept, the bank acts as the customer's wakil (agent) for an agreed-upon wakil fee. Corporate banking, the bank provides financing to its corporate clients through *Shariah*-compliant instruments, such as Goods and *Commodity Murabaha, Ijara,* and financing for small and medium-sized enterprises in cooperation with Damu Entrepreneurship Development Fund JSC. Additionally, the bank offers a range of cash services, including account opening, cash transactions, treasury services, and foreign currency exchange, to its corporate customers. The main sectors of the economy, such as agriculture, mining, infrastructure, trade, health, transportation, energy supply, and construction, are financed by the Bank.

Kazakhstan's regulatory framework for Islamic banking has historically been underdeveloped, resulting in challenges for *Shariah* compliance and national regulation. Reforms and updates to the regulatory environment are needed to develop support for the Islamic banking industry. In this case, Al Hilal Islamic Bank shall work with local authorities to adapt financial regulations to accommodate Islamic banking principles. Competition in the banking sector in Kazakhstan is dominated by traditional banks with well-established client bases and product offerings. In this regard, Al Hilal Islamic Bank has to find ways to differentiate its product offerings and compete effectively against traditional banks. Market awareness of the term Islamic finance is relatively new in Kazakhstan, and a significant challenge for the bank is educating and raising awareness among its potential customers and stakeholders. Economic factors, including the Inflation rate, the National Bank's base rate, and currency exchange rate fluctuations, pose risks for the bank's operations and profitability. With a regional market expansion, there is enormous potential for Islamic banking products and services among a majority Muslim population, where Al Hilal Islamic Bank will introduce a wide range of *Shariah*-compliant instruments for its potential customers. According to the market survey conducted by AIFC and CSQLaw, the current market demand by the corporate segment exceeds KZT 760 billion annually. The most widely used Islamic financial instruments are *Murabaha, Mudaraba*, and *Ijara,* with *Murabaha* accounting for approximately 90% of market demand (AIFC, 2024).

The government of Kazakhstan shows a high interest in promoting Islamic finance to diversify its oil-dependent economy. Al Hilal Islamic Bank may collaborate with the government and other financial institutions to foster and encourage the growth of *Shariah*-compliant financial solutions. In the innovation of financial services, banks should utilize financial technology and offer digital banking services, thereby improving the overall customer experience with innovative banking solutions. Al Hilal Islamic Bank faced significant challenges in positioning itself in the emerging Islamic banking sector of Kazakhstan. Nevertheless, the Bank capitalized on the growing demand for Islamic finance in Kazakhstan and the CIS region by implementing strategic initiatives that focused on regulatory cooperation, market education, and innovative product development. The success of the first Islamic bank of Kazakhstan was due to its ability to manage economic fluctuations, differentiate from traditional banks, and leverage government support to foster growth and market penetration.

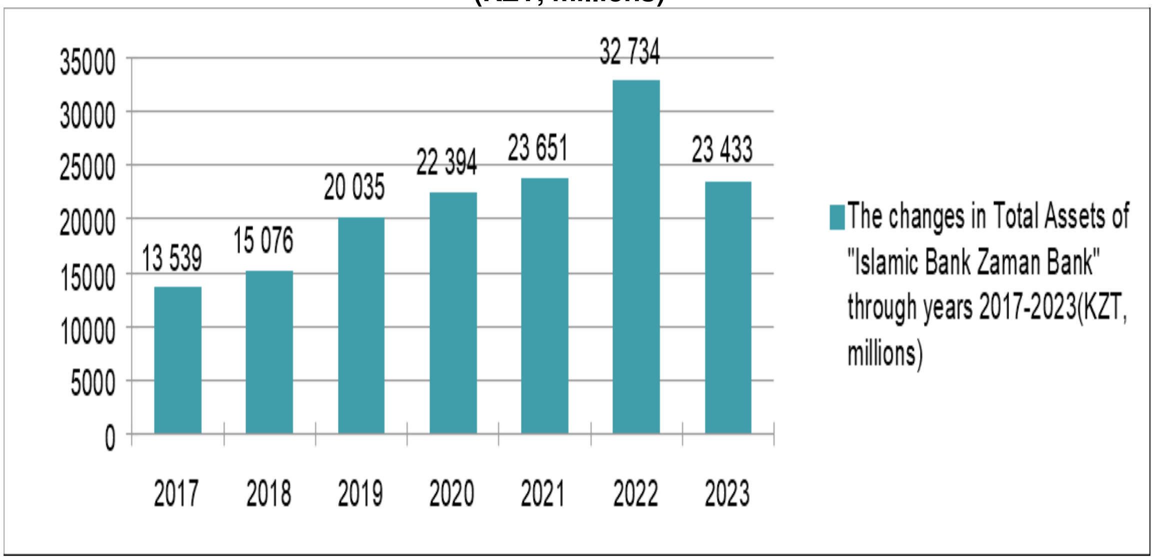
Zaman Bank

Zaman Bank's transition to Sharia-compliant banking showcases the potential and challenges of converting a conventional bank into an Islamic bank. Zaman Bank was established in 1991 as one of the oldest banks in Kazakhstan. The Bank got a permit for conversion into an Islamic bank from the National Bank of Kazakhstan on July 13, 2016. Lately, Zaman Bank received a license for its operations in accordance with Shariah principles and was renamed Islamic Bank Zaman Bank on August 17, 2017. After becoming a full member of the Malaysian commodity stock Bursa Malaysia, the Bank opened a representative office in Astana International Finance Center in 2018.

Zaman Bank is widely recognized as a pioneer in the development of Islamic banking in Kazakhstan. Established initially as a conventional bank, it received official approval in 2017 to fully transform into an Islamic bank, making it the first Islamic bank in Kazakhstan. This transition marked a significant milestone in the country's Islamic finance history, demonstrating the government's commitment to diversifying its financial system through Shariah-compliant models. The main shareholder of the Bank is the Islamic Corporation for the Development of the Private Sector (ICD), which is a group member of the Islamic Development Bank Group. The Bank is a partner of the Shariah Review Bureau, a global company specializing in compliance with Shariah principles. Islamic Bank Zaman Bank is a bank that targets its clients, including SMEs and individuals.

Zaman Bank is more than just a financial institution; it is a symbol of the viability and potential of Islamic finance in Kazakhstan. Its establishment underscores the government's ambition to position the country as a regional hub for Islamic finance in Central Asia, particularly through the *Astana International Financial Centre (AIFC)*, which serves as a gateway for international Islamic financial institutions. The Total Assets, as shown on Diagram 4, increased to 32.734 billion KZT in 2022 and then decreased to 23.433 billion KZT in 2023.

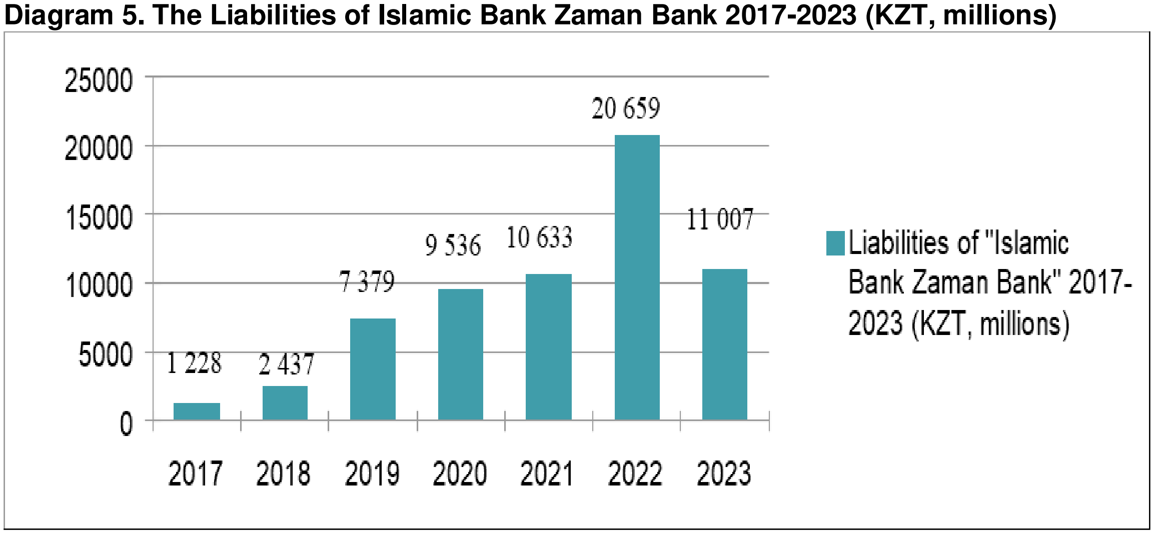
Diagram 4. The Total Assets of Islamic Bank Zaman Bank through years 2017-2023 (KZT, millions)



Source: Compiled by author, "Islamic Bank Zaman Bank" Audit reports

The growth of Liabilities to 20.659 billion KZT is shown in Diagram 6 for 2022, after which it decreased to 11.007 billion KZT in 2023.

Diagram 5. The Liabilities of Islamic Bank Zaman Bank 2017-2023 (KZT, millions)



Source: Compiled by author, "Islamic Bank Zaman Bank" Audit reports

The Liquid Assets to Total Assets ratio improved to 51.7 percent in 2022 and then decreased to 28.3 percent in 2023, as shown in Table 4. The slight decrease in the Capital to Total Assets Ratio is seen to amount to 53 percent in 2023, as shown in Table 4.

Table 4. Liquidity Ratio

Capital Ratio (%)							
Particulars	2017	2018	2019	2020	2021	2022	2023
Capital Luquidity Ratio	90,9	83,8	63,2	57,4	55,0	36,9	53,0

The ROE and ROA of the Bank fluctuated in 2022, remaining at 7.6 percent and 2.9 percent, respectively. (Table 4)

Table 5. Profitability Ratio

Profitability Ratios (%)							
Particulars	2017	2018	2019	2020	2021	2022	2023
ROE	5,6	4,1	1,3	1,6	1,2	7,6	0,1
ROA	5,1	3,5	0,8	0,9	0,7	2,9	0,0

Source: Compiled by author, 2025

The Bank offers Islamic banking products to its private clients and businesses in accordance with *Shariah* principles. The range of *Shariah*-compliant products includes Mudaraba investment deposits, Current deposits, Ijara leasing programs, and wakalah agency agreements. The main characteristic of the bank's activity is prohibiting any deals with businesses related to alcohol production, drugs, tobacco, gambling, and illicit entertainment. The regulatory environment remains a challenge for the Kazakhstani Islamic banking sector. Zaman Islamic Bank is also facing challenges in navigating regulatory requirements while ensuring compliance with local laws and Shariah norms. There is a need for more robust regulatory guidelines specific to Islamic finance, which can impede banks' operations and stifle their growth. The general public's acceptance of Islamic finance principles and benefits is limited. The Bank shall invest in educational campaigns and programs to raise awareness and promote the benefits of Islamic banking.

Product development presents a challenge for banks to design financial products that comply with *Shariah* rules while remaining competitive with their conventional counterparts. The growing demand for high-interest and market demand for ethical and Islamic banking solutions among the country's Muslim population is highlighted in a recent survey conducted by AIFC and CSQ Law's market survey. Zaman Islamic Bank has the opportunity to capture a significant market share by catering to this niche. Strategic partnerships and collaboration with international Islamic finance institutions can bring expertise, innovation, and investment to the Zaman Islamic Bank. Such alliances can enhance the bank's product range and expand its operations both domestically and regionally in Central Asia. Investing in digital banking solutions can boost Zaman Bank's operations to a broader client base through technological advancements. Digital platforms facilitate easier access to Islamic banking products in rural areas. Zaman Islamic Bank's experience in the Kazakhstani banking sector highlights the challenges of operating within an evolving regulatory framework, while also emphasizing the potential for expansion through strategic innovation and collaboration. The Bank aims to strengthen its position as a leader in the Islamic banking sector by prioritizing education, developing new products, and leveraging technology.

After examining the case of two Islamic banks operating according to *Shariah* in Kazakhstan, it can be concluded that the necessity of opening an Islamic bank at the state level exists. Kazakhstan is the sixth-largest wheat producer in the world, and the total value of Kazakhstan's agricultural output was approximately $17.8 billion in 2023, accounting for 5.1% of Kazakhstan's economy. Investment projects worth $ 353 million have been launched. (Sakenova, 2023). For Kazakhstan's government to support the agricultural sector of the economy, it is highly advisable to establish a State Agriculture Bank that implements Islamic

Finance instruments, which enable sustainable economic development of the country through halal practices. Developing social finance through *waqf* funds and zakat funds**.** In Kazakhstan, *waqf* and zakat funds operate under the umbrella of the Spiritual Administration of Muslims of Kazakhstan. However, the development of *waqf* investment funds on the AIFC platform is highly recommended. Moreover, Turkey's experience in this regard is crucial. *Waqf* funds were transformed in Turkey from the Ottoman Empire till.

In Kazakhstan, a two-tier banking system exists, with the Central Bank and the National Bank of Kazakhstan as the primary tier. Other second-tier banks in the country are corporate entities, regardless of their form of ownership, whose primary goal is to generate a profit. However, in Kazakhstan last year, following mergers and acquisitions, the number of corporate banks decreased from 38 to 21. The government of Kazakhstan consistently supports the country's banking sector against default and writes off non-performing loans for its citizens. In the country, the nation's debt burden is very high. In Conclusion, the development of National Islamic banks is crucial, or there are alternative ways to convert or nationalize existing banks, such as "Halyk Bank" JSC (People's Bank of Kazakhstan) or "Kaspi Bank" JSC, into fully fledged Islamic banks step by step. By the method of reasoning other it is called Ijtihad in Islamic Law of Contracts, it can be concluded as this: to respond to the demand of Muslim population in Kazakhstan (70% of Kazakhs identify themselves as Muslims) and to preserve national identity of Kazakh people, these two banks "Halyk Bank" JSC and "Kaspi Bank" JSC should be nationalized by the example of 100 % state owned Turkish banks as "Halk Bank" and "Ziraat Bank".

CONCLUSION

Islamic finance in Kazakhstan presents significant opportunities for economic diversification and growth. However, addressing the challenges of regulatory alignment, market development, and consumer awareness is crucial for the successful integration of this into the financial system. Continued support from the government, combined with strategic partnerships and innovative solutions, can propel Islamic finance to become a cornerstone of Kazakhstan's financial sector. In summary, the discussion in this research has revealed that Kazakhstan has made significant progress in implementing Islamic finance in a relatively short period. However, it is essential to highlight that there is still much to be done for Kazakhstan to benefit from the advantages of Islamic finance fully. While the future appears promising, certain obstacles lie ahead, and market participants and regulators need to take concrete steps to support market takeoff. Enhancing the regulatory framework to support the growth of Islamic finance while ensuring consumer protection. Islamic finance departments at each regulatory and supervisory authority must be established in Kazakhstan. Promoting awareness and education: Launching educational campaigns and training programs to increase awareness and understanding of Islamic finance. Organizing conferences and workshops among students by inviting well-known scientists and practitioners in the Islamic finance industry. Opening up Islamic finance qualifications and programs at local universities by collaborating with worldwide Islamic finance centers and universities. Raising awareness through mass media and TV programs. Training centers must be established to enhance the skills and knowledge of existing professionals in the Islamic finance industry and to certify them. Supporting innovation, encouraging the development of innovative Sharia-compliant financial products and services. Implementation of projects in the information technologies and digitalization of the country through Fintech companies that comply with Shariah rules. Fintech companies shall develop a digital framework that integrates Islamic virtual banking, enabling Islamic finance institutions to offer digitalized financial services to their clients.

Fostering international collaboration, building partnerships with established Islamic finance hubs like the Dubai International Financial Center and the Malaysian International Financial Center to share knowledge and best practices. Opening Islamic finance centers at university levels in collaboration with the world's best universities, like Durham University's Islamic Finance Department, Harvard, Cambridge, and Oxford Islamic finance centers, which have already developed their programs and research in the Islamic finance industry, and can positively contribute to the further development of Islamic finance studies in Kazakhstan and prepare qualified professionals in this field. Moreover, joint programs with international universities offering Master's and PhD degrees in Islamic finance should be established, enabling students to obtain dual diplomas. Islamic banking windows can develop the necessary legal framework that allows Conventional banks to open Islamic windows, thereby fostering the inclusion and prosperity of the Islamic finance industry in Kazakhstan. A legal framework for Islamic windows must be introduced. AIFC must develop necessary regulatory frameworks and *Shariah* requirements that enable the opening of Islamic windows, encouraging the participation of local banks in the Islamic finance industry.

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