

The importance of digitalization of the Islamic finance

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Abstract

This article will consider the trends of digitalization of Islamic financial instruments. In the current realities, digitalization concerns all branches of human activity. The most important resource for making any decisions is information, and the key factor in this area is the speed of processing and exchange of information. To achieve such goals, new systems for collecting, transmitting, and processing information are being created every day. To understand the scale of changes in the market of financial instruments, the authors conducted studies of changes in the number of digital products in the financial market of Kazakhstan. This trend is also observed in the world market, of which Kazakhstan is a part. Considering that the main engine of any market is the consumer, the authors conducted a study on the change in the number of users of digital products and transactions. From the studies obtained, it follows that for the successful implementation of Islamic finance tools, it is necessary to adhere to the trends that are observed in the market.

Keywords. Islamic finance, digitalization, payment cards, Islamic cards.

JEL codes: G01, G20, G21

1 Introduction

We live in an age of information and technology. As Winston Churchill said, "Whoever owns the world owns the information." The most expensive resource of the twenty-first century is information. And the key factor in using this resource is the speed of receiving, processing, and transmitting the information. This is the most important aspect that decides a lot in our time. It is important to understand these skills concerning information are important in all sectors and levels of human activity. Touching on the topic of digitalization in all industries, we would like to focus on finance. This industry is one of the most advanced in the field of digitalization. It is understandable, the science of the most liquid asset needs a special approach.

68% of the world's business leaders call digital transformation a top priority for their companies. The COVID-19 pandemic played an important role here. Organizations were forced to adapt to new realities: to transfer

employees to remote work, and to revise the approach to service and document management.

The financial sector was one of the first to introduce information technology into work. Over the past 10 years, applications have appeared that allow to perform some operations without leaving home. And even online banks that do not have branches at all. The development was slow and only in 2020 the digitalization of banks began to develop faster — otherwise, it was impossible to keep customers in the new conditions. As a result, the companies that managed to pick up the trend were the winners.

Against the background of the spread of COVID-19, the financial markets were dealt a severe blow, which caused the whole world to have an urgent need to rethink the system and introduce new tools [6].

One of the indicators of successful digitalization of finance is still payment cards. In our country, every year more and more people are switching to digital methods of payments and money transfers. We can consider in more detail the data on the payment card market of Kazakhstan. During the research, the authors carried out an analysis of the payment transaction market of the Republic of Kazakhstan. In this article the statistical data of the National Bank of the Republic of Kazakhstan were considered. From where the current data concerning the payment transaction market were taken.

2 Literature review

The purpose of this review is to clarify all the existing trends in the financial market in order to forecast the further course of all events. To achieve these goals, the authors conducted data analysis on open sources.

It was done a review of statistical data on the website of the National Bank of the Republic of Kazakhstan. This resource is the most top-end and accurate data bank. The authors analyzed data on changes in the number of ATMs and digital terminals. The following resources used by the authors is the website kursiv.kz. From this source, the authors analyzed the state of the global financial market after covid restrictions. Information was taken from this resource that the coronavirus pandemic accelerated the digitalization process. More detailed data on the trend change in the financial market of the world were observed in the EU and CIS countries. As for Islamic finance, the growth of Islamic banks also implies an increase in interest from users, as discussed in this resource.

To review the Kazakh market of Islamic finance, the authors took data from the Kazakh Islamic financial website [tayyab](http://tayyab.kz). This service is one of the services that carry out financial services activities on the territory of Kazakhstan. The authors analyzed the state of users of Islamic financial products. The set goals were achieved by analyzing data from the resource.

Also, from the results obtained, it became clear that the number of users of Islamic financial services is increasing every year. It was not without an analytical report from PwC. Data on the change in the number of users of digital payment methods was obtained from this journal. In the financial market of Kazakhstan, there is an increase in favor of digital payment methods and money transfer, which also include subjects of Islamic finance.

3 Methodology

Statistical and comparative methods of analysis were used in this study. The initial data and financial reports of the organization were obtained from open sources. The authors conducted a comparative analysis of data changes in comparison with the reporting date and previous years.

4 Results and discussion

As of September 01, 2022, 61.8 million payment cards are in circulation. The most common are debit cards, whose share is 78.39%, and the share of credit cards is 18.51%. Debit cards with a credit limit and prepaid cards account for 3.10%. In August 2022, the volume of transactions using payment cards of Kazakhstani issuers amounted to 11.4 trillion tenge, the number – 810.1 million transactions. At the same time, compared to the same period in 2021, the number of non–cash transactions increased by 33.3% and reached up to 788.1 million transactions, the volume - by 39.8%, reaching 9.5 trillion tenge. The holders of payment cards carried out 21.9 million cash withdrawal operations for 1.9 trillion tenge. There is a decrease in the number of cash withdrawal operations compared to August 2021 by 1.1%. At the same time, the volume of cash withdrawal operations increased by 7.1%. The main share of non-cash transactions in Kazakhstan is carried out via Internet /mobile banking (64.5% of the total number of transactions and 82.4% of the total volume of non-cash payments and money transfers) and POS terminals (35.5% and 17.3% of the total number and volume of non-cash payments and money transfers). Cash withdrawal operations were mainly carried out through ATMs (98.9% and 91.0% of the total number and volume of cash withdrawal operations). [1].

From the first table, we can understand that the market for plastic cards in Kazakhstan is growing very fast. The population of Kazakhstan prefers electronic payment systems. This is confirmed by an 89% increase in the number of payment acceptance terminals in one year. It is also worth paying attention to reducing the number of ATMs. This means that people have started to cash out less often. Which can also have a positive impact on the fight against the shadow economy and corruption distortion in general [5].

Table 1. Kazakhstan payment card market

Indicators	01.09.2021	01.09.2022	Change	Change in %
Number of cards in circulation (thousand units), including:	55 745,70	61 777,60	6 031,90	10,8
- Local systems	18 164,30	20 952,70	2 788,40	15,4
- International systems, including:	37 581,40	40 824,90	3 243,50	8,6
- Visa International	27 130,50	30 962,90	3 832,40	14,1
- MasterCard Worldwide	8 659,80	8 217,20	-442,60	-5,1
Number of POS terminals (pcs.), including:	356 258	674 033	317 775,00	89,2
Number of ATMs (pcs.), including:	12 771	12 570	-201,00	-1,6

As for Islamic bank cards, their market share in Kazakhstan is significantly small, but in recent years there has been a significant increase. For example, as of February 2023, the first Islamic fintech of Kazakhstan, Tayyab, issued its one hundred thousandth card. If we take into account the data for September 2022, this entity accounts for only 0.1% of the market share. However, if to look at the launch date of the project itself from July 2021, the company has issued 100,000 cards in a year and a half. Based on this situation, the question arises whether Islamic fintech companies should enter the market of Kazakhstan [3]. Worth it, because the number of online banking users is growing every day. For a more detailed overview, let's pay attention to the overview of the payments market.

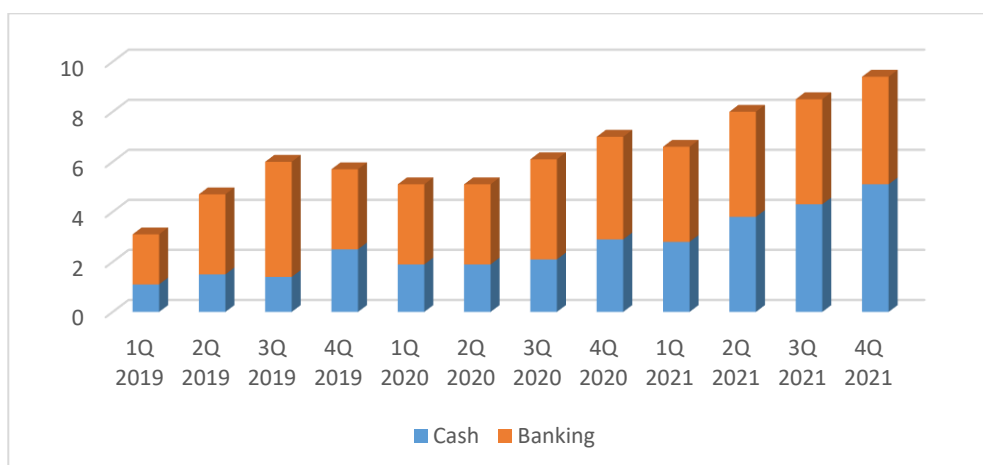


Figure 1. Dynamics of changes in the volume of payments by quarter, trillion tenge

Over the period from 2019 to 2020, the cash payments market has seen a general trend of growth by an average of 8% quarterly. A similar trend is observed in non-cash payments, but with a faster growth rate, on average by 14% quarterly. At the same time, abnormal jumps in growth and falls are observed in 2020, which is explained by the COVID-19 pandemic and a change in consumer preferences [10].

The pandemic led to a worldwide quarantine, restrictions affected almost all small and medium-sized businesses, which led to market stagnation in the second quarter of 2020. However, this situation provoked delayed demand and an active transition to online, which led to a significant increase in payments in the third and fourth quarters of 2020 by 19% and 15%, respectively.

The market shows a general trend to increase the number of payments in Kazakhstan. In 2021, the amount of cash payments increased by 31%, and non-cash payments by almost 2.5 times compared to 2019. Cash settlement in 2019 was used to pay for goods for 13.8 trillion tenge, which accounted for 70% of all retail payments. However, 2020 and 2021 showed a trend for a decrease in the use of cash as a percentage of the total volume - 66% and 55%. Accordingly, the share of non-cash payments grew. The average amount of cash withdrawals increased by 84% in 2021 compared to 2019, which most likely indicates an increase in wages and a decrease in the frequency of cash withdrawals from ATMs. At the same time, the average check for non-cash payments decreased by 7%. The change in the average check is justified by an increase in the total amount of payments in the Republic of Kazakhstan, as well as a multidirectional trend in the number of transactions. From 2019 to 2021, cash withdrawal transactions decreased by 17%, and non-cash transactions increased by 168% [4].

The rapid growth of non-cash payments is due to changes in consumer demands and the emergence of new payment technologies. According to data for 2021, the amount of non-cash payments amounted to 14.5 trillion tenge, which is 82% more than the value of 2020. At the same time, in 2020, the increase relative to 2019 was at the level of 37%. It is worth noting that the frequency of payment (the number of transactions) via cashless settlement is also growing, as indicated by an annual increase in 2020 and 2021 of 34% and 77%, respectively

Although the COVID-19 pandemic and restrictive measures accelerated the transition from cash payments to non-cash payments, the active demand for non-cash payment methods began earlier: since the first quarter of 2019, we have seen an increase in the amount due to pay via POS terminals. According to the NBRK, in 2019, the number of offline POS

terminals increased by 27%, from 126 thousand to 161 thousand, which may mean an increase in demand for card payments. Already in 2019, the amount of non-cash payments accounted for one-third of the total payments market.

The worldwide lockdown, the boom in online deliveries, remote work, the development of retail e-commerce and the spread of innovative technologies have made their own changes in consumer behavior. The decrease in the amount of payments in the first half of 2020 was due to the initial economic shock and job losses. One of the confirming factors is the decrease in the level of employment of the population to a minimum value of 65.7% over a 17-year period. However, by the end of the second half of 2020, growth is noticeable, which continues its trend in 2021. Despite job cuts and unemployment, caused by the closure of many small and medium-sized businesses in 2020, nominal revenues by the end of the year, namely in the 4th quarter, increased by 15.5% compared to the previous quarter, due to which a strong growth of 27% can be justified [2].

The new crisis caused by the COVID-19 pandemic has provided the basis for creating a safer and more sustainable payment system. Many market participants have adapted to the new conditions through digitalization, improved their business models and processes, and expanded the range of services and services offered. As a result, these factors helped to create greater consumer confidence in online purchases, which can be observed from the growth in the share of non-cash payments through online POS terminals in the second half of 2020. In 2021, the trend for convenience and safety continued. New ecosystems with multi-vector consumer services are being created, thereby covering an increasing market share (Figure 2).

The amount of online payments has increased 2.9 times since 2019, and the number of transactions has increased 2.7 times due to the changed consumer behavior - people began to trust online purchases more. Other reasons for this growth were: the successful introduction of mobile commerce and banking ecosystems, the development of delivery services and incentive systems such as cashback [9].

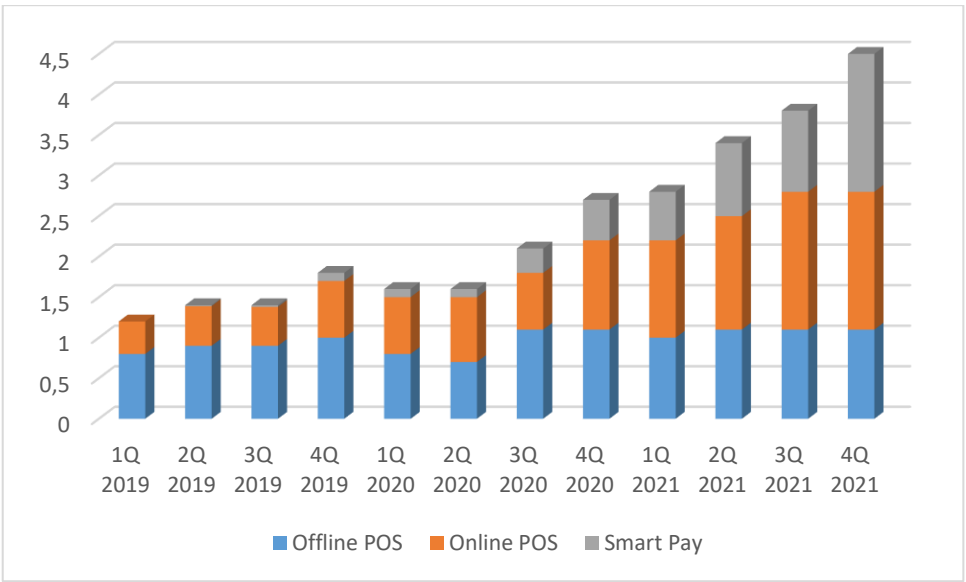


Figure 2. Dynamics of changes in the volume of payments by quarter, trillion tenge

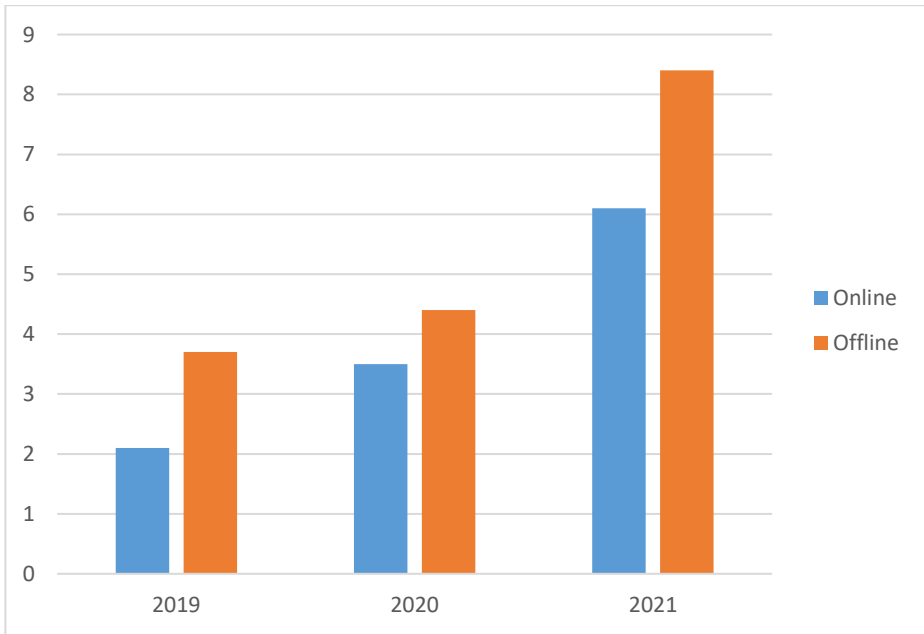


Figure 3. Change in the amount of non-cash payments from 2019 to 2021

Despite the rapid development of the online market, there is also a significant 2.3-fold increase in the amount of offline payments from 2019 to 8.4 trillion tenge and 2.6-fold increase in the number of transactions to 1.4 billion. However, it can be noted that the largest jump in the amount of non-cash payments is mainly accounted for by Smart Pay* with a maximum annual growth of 6.4 times over a two-year period. This trend is caused by the convenience and security of users, as well as mass availability to pay with the use of new technologies (Figure 3) [7].

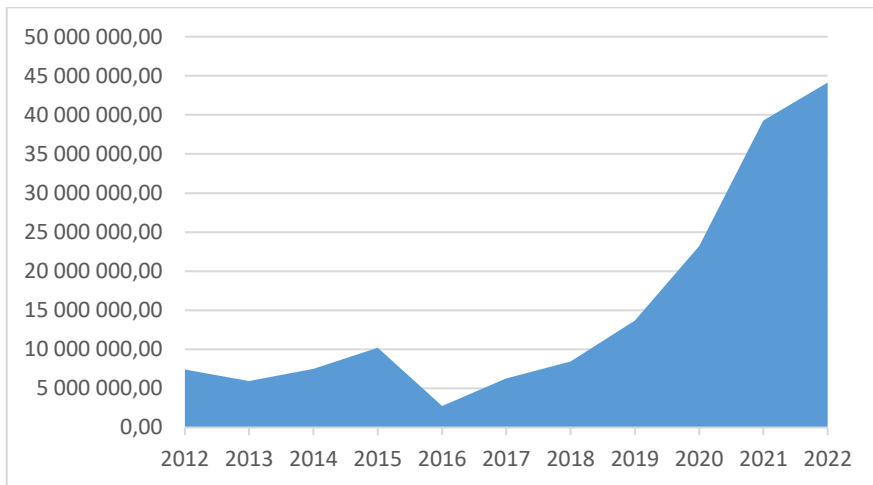


Figure 4. Change in the Murabaha asset portfolio

Given the excellent potential of the Kazakhstani market, it can be assumed that this market has a strong potential for the entry of various Islamic fintech projects. The most important open question in this situation is how Islamic banks live in this market. To do this, it is needed consider the portfolio of an existing Islamic bank in Kazakhstan (Figure 4). The diagram shows that the bank's portfolio is growing, which means that the bank is developing. And against the background of other financial entities, the bank can exist quite well [8].

5 Conclusion

According to the conducted research, it can be concluded that digitalization is very important for all industries and doubly so for the finance sector. The analysis of payment systems of Kazakhstan was carried out. The result shows that online payment and money transfer methods are beginning to prevail. An analysis of Islamic banks was also carried out. There are practically no Islamic banks in this market, but this does not mean that there are no prospects for Islamic banks in the market. An analysis of the portfolio

of Al Hilal Bank was carried out, which showed that the bank has a noticeable growth. Thus, we came to the conclusion that the financial market of Kazakhstan is developed in terms of digitalization, and if Islamic financial companies want to introduce themselves and compete with other banks, they need to digitalize their products, since every year more and more people make a choice in favor of online.

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