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How Essential Are Social Goals for Islamic Banks in Indonesia?

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ABSTRACT

Islamic banking in Indonesia is expected to play a significant role in addressing social welfare, as envisioned by the principles of Maqasid Sharia. However, there remains an ongoing disparity between its financial achievements and societal contributions. While the industry has shown considerable progress in profitability, its broader societal objectives, such as promoting falah—a holistic state of community well-being—remain insufficiently realized. This study examines the extent to which Islamic banking organizations in Indonesia have achieved their societal objectives, focusing on their alignment with the principles of Maqasid Sharia and the pursuit of falah. Despite its financial success, previous research highlights the persistent challenges Islamic banks face in fully realizing their intended societal impact. The adoption of the Islamic Social Banking (ISB) framework is proposed as a viable solution to bridge this gap. This framework provides a targeted strategy for aligning financial operations with social welfare goals. By adopting ISB, Islamic banks can balance profitability with delivering tangible benefits to society, ensuring alignment with Islamic values. This study further underscores the policy implications for regulators of Sharia banking in Indonesia, emphasizing the need for updated legislation and incentives to promote socially responsible practices. These measures can enhance customer trust, support industry initiatives, and foster sustainable development. By adopting the ISB framework, Islamic banks in Indonesia have the potential to redefine their role in the financial sector, shifting from a profit-centric approach to one that emphasizes societal well-being, ensuring that social welfare remains a central focus of the industry's growth.

Keyword: *Islamic Banking, Islamic Social Banking, Maqasid Sharia, Well-Being.*

Introduction

Islamic banking serves as a vital intermediary for persons who have excess assets and others who require financial resources (Fauziah, 2021). Islamic banking ensures assurance and security for its consumers by refraining from banned behaviors such as maysir, gharar, and riba (Mohd Nor, 2016). Within this framework, the implementation of Islamic banking serves not only as a financial institution, but also as an advantage for the Muslim population. Furthermore, Islamic banking not only plays a role in boosting financial inclusion from an economic perspective, but it also indirectly helps to enhancing social well-being (Ahamat, 2017). Islamic banking plays a vital role in fostering a more sustainable lifestyle for the Muslim community by providing lawful financial services and facilitating economic operations that adhere to religious principles (Rahmah et al., 2023).

Islamic banking is a financial system that operates according to the principles of Islamic law, characterized by the prohibition of riba and the emphasis on profit and loss sharing (Abbas & Arizah, 2019). The concept of Profit and Loss Sharing is based on the notion of *al-ghounm bi al-ghourm*, which signifies that obtaining profit is only justified through economic endeavour (Hamza & Ben Jedidia, 2014). Under this approach, neither party is solely responsible for incurring losses, as the source and recipient of funds must distribute risks and losses in accordance with the predetermined agreement. The objective is to improve equity and justice in society through this technique (Khan, 2010).

Although Islamic banking has had substantial expansion and improvement in recent times, it nevertheless faces extensive criticism due to perceived deficiencies in achieving favorable social results (L. Hamidi & Worthington, 2021). Scholars are not satisfied with how well Islamic banks are doing in terms of reducing poverty and improving the overall welfare of society. According to Mansoori (2011), Islamic banks have not succeeded in accomplishing the goal of equitable distribution of wealth in society. Criticisms stem from the perception that Islamic banking is rooted on materialism rather than adhering to the ideals of Maqasid al-Syariah. According to critics, the primary objective of Islamic banking is to create wealth under the guise of Islam (Khalil & Hussain, 2022).

This article seeks to assess the degree to which Islamic banking in Indonesia has successfully accomplished its societal objectives. Moreover, the article will outline measures that may be used to improve the attainment of social objectives in the Islamic banking industry in Indonesia, through a comprehensive review of pertinent literature and research discoveries.

Methodology

This study employs a qualitative research methodology to assess how far Islamic banking in Indonesia has achieved its societal objectives. The research process involves a comprehensive review of existing literature, reports, and studies related to the performance and social goals of Islamic banking institutions. The methodology is designed to gain a holistic understanding of the extent to which Islamic banks in Indonesia are aligning with their ethical and social principles. The primary method of data collection involves reviewing academic journals, industry reports, policy papers, and regulatory documents related to Islamic banking in Indonesia. The literature review includes works from reputable sources in Islamic finance, banking, and socio-economic development.

Findings and Analysis

1.1 Issues in Social Objectives of Islamic Banks in Indonesia

L. Hamidi & Worthington (2021) conducted research to evaluate the degree to which Islamic banks in Indonesia have accomplished their social goals. This assessment was based on four social indicators: Islamic perspective; Kinder, Lydenberg, Domini Research and Analytics index of corporate social performance (KLD Indices); The 17 Sustainable Development Goals (SDGs), and ESG Scorecard (Environmental, Social, and Governance). This research assessed the yearly reports of 26 Islamic banks in Indonesia, which included 12 Islamic Commercial Banks, 7 Islamic Business Units, and 7 Islamic Rural Banks.

According to the research findings, with the exception of BMI and BCA Syariah, all Islamic Commercial Banks have shown an improvement in their social result ratings between 2015 and 2016. The highest social result performance is only three Islamic Commercial Banks, specifically BNI Syariah, BTPN, and Bank Syariah Mandiri, fulfill the requirements of being proactive and proficient in anticipating social duties. There are total of 4 banks in the Islamic Business Units category that have accommodating status, meaning they fulfill all the necessary requirements. Additionally, there are 2 banks with proactive status and 1 bank with defensive position. Meanwhile, all of the Islamic Rural Banks that were evaluated either have a reactive status or are performing below the acceptable level. Therefore, this research suggests that not all banks in Indonesia sufficiently satisfy the social aspects. However, Islamic banking has progressively enhanced its ability to accomplish its social aims. Nevertheless, occasionally, the consequences indicate a lack of concern or willingness to prioritize goals pertaining to consumers and the environment.

Islamic banking is currently perceived to have a more positive impact on wealthier communities through Islamic financial services such as zakat and qardhul hasan compared to those who are less fortunate (Mergaliyev et al., 2021; Zaman et al., 2009). Nevertheless, Indonesia encounters a substantial obstacle in the shape of poverty, which is anticipated to be tackled by the proactive involvement of Islamic banking. However, Islamic banking seeks to do more than just promoting economic development by giving credit. It also takes into account the income aspect while distributing loans. Islamic banking effectively carries out a process of credit allocation by establishing its credit objectives. In general, banks often extend loans only to enterprises that are considered bankable and feasible which means they have a strong grasp of banking operations. As a result, Islamic banking operations often do not consider disadvantaged populations as a target market for market segmentation. Consequently, Islamic banking has problems with effectively reaching out to restricted populations in order to offer qardhul hasan loans, which might impede endeavors to enhance the welfare of these communities.

1.2 Reviewing measures to overcome the shortcomings of Islamic banking

In order to fulfill the social objectives of Islamic banks, it is imperative to concentrate on formulating an Islamic banking framework that can effectively promote socio-economic prosperity and human welfare by mitigating poverty and inequality (Khalil & Hussain, 2022). Hence, it is necessary for Islamic banks to give precedence to the attainment of societal objectives above individual goals by taking into account Maqasid al-Shariah. This vision aims to promote the well-being of different sectors of society, which is crucial for the establishment of a welfare-focused framework that can effectively include moral values and social justice regulations (Yusof et al., 2009). According to Imam Al-Ghazali (d. 505H/1111M) in Khalil & Hussain (2022), Maqasid al-Shariah may be described as the primary objective of Shariah, which is to enhance the welfare of society by protecting their religious beliefs (din), physical well-being (nafs), intellectual capabilities (aql), future generations (nasl), and financial wealth (mal). Any measure that guarantees the preservation of these five aspects is beneficial for the collective welfare and is considered desirable, while any action that undermines them is detrimental to the common good and should be eliminated.

This research supports Asutay's perspective Asutay (2007), that it is essential to establish Islamic social banks in order to tackle the social shortcomings of Islamic banks. By incorporating the concepts of social banking (SB) into their operations, Islamic banks are anticipated to strengthen their ability to grow and promote social fairness. Islamic social banks are expected to allocate additional cash to uplift underprivileged communities and back various social initiatives, guided by these principles.

The research conducted by M. L. Hamidi and Worthington (2018) offers more elaboration on the notion of Islamic social banking. During the debate, social banking (SB) is defined by its aims, which are determined by the notion of the "triple bottom line" comprising of Prosperity (sustainable profitability), Planet (environmental stability), and People (social purpose). Subsequently, the research introduces a further "P," namely Prophet. The latter encompasses all aspects pertaining to Sharia law, as instructed by Prophet Muhammad (PBUH), which must be followed by all Islamic financial organizations. This notion exemplifies both logical coherence and direct applicability to the Sustainable Development Goals (SDGs). Islamic social banking can be accomplished by the integration of Islamic banks (IB) with certain modifications in emphasis. This integration results in the formation of a unified institution known as Islamic social banking (M. L. Hamidi et al., 2023).

This research indirectly supports the presence of Islamic social banking in Indonesia by highlighting its potential role in fostering not only economic development but also social and environmental accountability. Islamic social banking represents a model that integrates ethical banking principles with a focus on societal well-being, thereby extending beyond the traditional profit-maximization focus of conventional banks. The adoption of Islamic social banking is particularly relevant in Indonesia, where there is a growing need for financial institutions to align their operations with the principles of Maqashid Sharia, which emphasize social justice, fairness, and environmental stewardship.

Furthermore, by integrating the CSR framework and supporting the achievement of the SDGs, Islamic banks can position themselves as key drivers of sustainable finance. This shift reflects a global trend in which financial institutions are increasingly being called upon to address broader societal challenges, such as poverty alleviation, inequality reduction, and environmental sustainability. The emphasis on social and environmental accountability in Islamic social banking ensures that banks not only comply with Shariah principles but also contribute to long-term societal and environmental goals.

In addition, Islamic social banking offers a framework for financial institutions to foster greater financial inclusion, particularly for underserved populations. By providing Shariah-compliant financial products and services, these banks can promote economic participation among marginalized groups, thus contributing to poverty alleviation and economic empowerment. Therefore, the integration of Islamic social banking into Indonesia's financial system can help bridge the gap between economic development and social responsibility, promoting a more holistic and sustainable approach to banking in line with Islamic values.

Closing

In conclusion, the introduction of Islamic Social Banking (ISB) in Indonesia offers a promising solution to bridge the gap between profit maximization and the fulfillment of social objectives. By incorporating the triple-bottom line—prosperity, social responsibility, and environmental sustainability—ISB promotes not only financial stability but also societal and environmental well-being. This model aligns closely with the principles of Maqashid Sharia, ensuring that Islamic banks fulfill their ethical obligations while contributing to long-term sustainability goals. Furthermore, ISB has the potential to enhance financial inclusion, reduce income inequality, and support underserved communities, positioning Islamic banks as key players in achieving inclusive socio-economic growth in Indonesia. As global attention shifts toward sustainable finance, ISB can serve as a model for ethical banking that balances profitability with the greater good, reinforcing the role of Islamic banks in fostering a more equitable and sustainable future.

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