

**How to Cite:**

Lotfi, Z. N. (2024). Islamic finance as an alternative for financing the Algerian economy post-COVID-19. *International Journal of Economic Perspectives*, 18(6), 1008–1035. Retrieved from <https://ijeponline.org/index.php/journal/article/view/610>

## Islamic finance as an alternative for financing the Algerian economy post-COVID-19

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**Abstract**---In this article, we focus on Islamic Finance, which offers a unique and ethical alternative for financing the Algerian economy in a post-COVID-19 scenario. This system is based on principles derived from Sharia law, such as the prohibition of interest (riba) and investment in activities deemed unethical. By adhering to these principles, Islamic Finance promotes fairness, transparency, and risk sharing between parties. In the context of Algeria post-COVID-19, Islamic Finance can help stimulate economic growth by providing access to funding for businesses and individuals while minimizing exploitative practices. This alternative form of financing can also attract foreign investment, diversify the financial sector, and promote socio-economic development. Additionally, Islamic Finance mechanisms like Mudarabah (profit sharing) and Musharaka (partnership) can foster entrepreneurship and innovation in Algeria. Furthermore, Islamic Finance emphasizes real economic activities and asset-backed transactions, which can reduce speculation and promote stability within the Algerian economy. By encouraging ethical investments in sectors such as agriculture, infrastructure, and renewable energy, Islamic Finance can contribute to sustainable development and poverty alleviation in the country. Overall, embracing Islamic Finance as a financing alternative in Algeria post-COVID-19 cannot only help rebuild the economy but also foster a more inclusive and sustainable financial system aligned with Islamic ethical principles.

**Keywords**---COVID-19, Economic Crisis, Algerian economy, Islamic Finance, Islamic financial instrument.

## Introduction

The COVID-19 pandemic has severely affected economies worldwide, with countries struggling to revive economic activities disrupted by lockdowns and business closures. As governments explore different financing options to support recovery efforts, Islamic finance could offer an attractive alternative, particularly for Muslim-majority nations like Algeria (Mzoughi et al., 2022).

Islamic finance is a rapidly growing segment of the global finance industry, guided by the principles of Sharia (Islamic law). It prohibits interest-based transactions (riba), excessive uncertainty (gharar), and unethical practices like gambling and speculative trading. Instead, it emphasizes risk-sharing, asset-backed financing, and ethical investment in tangible assets and real economic activities (Abdul-Rahman & Gholami, 2020).

Several aspects of Islamic finance make it well suited for financing post-COVID-19 recovery efforts. First, its emphasis on equity-based financing and risk sharing aligns with the need for inclusive and sustainable economic growth. Islamic financial instruments like Mudaraba and Musharaka can help channel funds into productive sectors, creating jobs and stimulating economic activities.

Moreover, Islamic finance's focus on real assets and tangible economic activities can support infrastructure development, a crucial factor for economic revival. Instruments like sukuk (Islamic bonds) and ijara (leasing) can finance large-scale projects, promoting economic diversification and reducing reliance on oil and gas revenues.

Furthermore, Islamic finance's ethical principles promote financial inclusion, social welfare, and environmental sustainability – key considerations for a just and equitable recovery. Zakat (obligatory charity) and waqf (endowments) can support social safety nets and community development initiatives, mitigating the pandemic's adverse socioeconomic impacts (Biancone et al., 2022).

Algeria is also affected by the crisis and is facing an unprecedentedly difficult economic context due to various factors. With regard to the structural crisis that resulted from the decline in hydrocarbon prices and which ended with the coronavirus crisis, Algeria is in a difficult situation. Due to the low economic diversity, the main economy of the Maghreb is very vulnerable to fluctuations in oil prices. According to IMF projections, the economy of Algeria is expected to undergo a reduction of 5.2% in 2020 and present a budget deficit that ranks among the highest in the region. If the reforms are not implemented, the Algerian economy will suffer a recession and will have to face an inevitable need to borrow from foreign countries. All people affected by the pandemic, whether they are individuals or companies, need financial support. To face this challenge, it is necessary to use a variety of financial services, strategies, and technologies to establish a more sustainable post-COVID financial system for the Algerian economy (Pnud, 2020).

**Problem Statement**

With this in mind, we would like to ask in this article the following question: how can Islamic financial instruments provide solutions to overcome the negative effects of Covid-19? And to what extent can they accompany the recovery of the Algerian economy post Covid-19?

**Purpose**

The purpose of this article is to investigate whether Islamic finance could be a feasible means of supporting and revitalizing the Algerian economy in the wake of the COVID-19 pandemic. It is titled "Islamic Finance as an Alternative for Financing the Algerian Economy Post-COVID-19." This essay will examine the tenets and tools of Islamic finance and show how they can be applied to boost economic expansion, encourage entrepreneurship, and help Algeria's economy overcome its post-pandemic difficulties. It also aims to shed light on the infrastructure and legal framework needed to support the introduction of Islamic finance in Algeria, which will eventually aid in the country's long-term stability and economic recovery.

**Aims of this research**

The primary aim of this research is to explore Islamic finance as a viable alternative for financing the Algerian economy in the post-COVID-19 era. It seeks to analyze the potential benefits and challenges of adopting Islamic financial instruments and principles in the Algerian context. The study aims to evaluate the feasibility and implications of integrating Islamic finance into the existing financial system of Algeria.

It further intends to propose strategies and recommendations for policymakers and financial institutions to facilitate the implementation of Islamic finance. Additionally, the research aims to assess the potential impact of Islamic finance on economic growth, financial inclusion, and socio-economic development in Algeria. Ultimately, the goal is to provide a comprehensive understanding of Islamic finance's role in supporting the recovery and sustainable growth of the Algerian economy.

**1. The state of the Algerian economy**

The main driver of economic growth in Algeria is the hydrocarbons industry and government investments. The economic crisis caused by COVID-19 provides a useful way to understand the impact on the economy without the confusion caused by fluctuating exchange rates affecting hydrocarbon exports. In terms of fiscal revenues (60%) and gross domestic product (19%), COVID-19 has affected oil more than any other commodity traded on the stock market. Due to the spread of the virus in Algeria, GDP growth slowed from 1% in 2019 to 1.4% in 2019, reflecting the changes in hydrocarbon prices and the limited diversification of the Algerian economy. Since then, growth has also slowed in non-hydrocarbon sectors. Given that non-hydrocarbon growth rates decreased from 3.3% in 2018 to 2.6% in 2019, sectors like construction, public works, housing, agriculture,

and commerce have all experienced a slowdown. Several factors, including the growth of public and private investments, suggest that the Algerian economy continues to be heavily reliant on the hydrocarbon industry (Pnud, 2020).

Table 1. Economic indicators' evolution of the Algerian economy

Year	2019	2020	2021	2022
Growth PIB (%)	+0.8	-6.5	+3.8	+2.1
Non-Hydrocarbon Growth (%)	+2.4	-6.0	+3.6	+1.4
Inflation	+2.3	+2.1	+3.8	+4.2
Public Deficit	-9.6	-15.8	-12.9	-9.6
Current Deficit (%)	-10	-13.4	-12.9	-14.6
Foreign Exchange Reserves	+13.6	+13	+5.7	+3.0

Source: World Bank

## 2. The impact of COVID-19 on macroeconomic indicators of the Algerian Economy

### 2.1 External Sector

In response to the fall in hydrocarbon export earnings, authorities implemented measures to limit the expansion of the current account deficit. The authorities set an objective to cut the import bill by at least US\$10 billion, or 6 percent of GDP, notably through a local currency devaluation. Since the beginning of the year, the Algerian dinar has consequently lost value against the USD (-6.3 percent), the Euro (-9.2 percent) and the Yuan (-6.8 percent), leading to increased import prices. Other compression policies to have been introduced include the extension of import restrictions on vehicles that are older than three years. The Government is also taking measures to reduce the country's reliance on imports of services, ordering sectorial ministries to award contracts to domestic firms. The transfer of the Algiers metro management from the French RATP Group to an Algerian firm owned exclusively by the Metro of Algiers Company (EMA) to ensure full autonomy in the management and the operations and the maintenance of the local metro is a case in point. The current account balance remained unchanged, at US\$9 billion, in the first-half of 2020 compared to the same reference period last year, despite large variations in its components. Exports shrunk by 39 percent in H1/2020 compared to H1/2019, largely led by hydrocarbon exports falling to US\$10 billion in H1/2020, from US\$17 billion in H1/2019. Meanwhile, imports declined from US\$23.3 billion in H1/2019 to US\$18.1 billion in H1/2020 (22 percent) due to low domestic demand, import compression policies and the dinar's devaluation. Remittances and international tourism receipts are expected to have fallen. The authorities estimate that US\$2–3 billion remittances are circulating through the banking system every year, with the World Bank projecting remittances to have contracted by 8 percent in 2020. Losses in international tourism

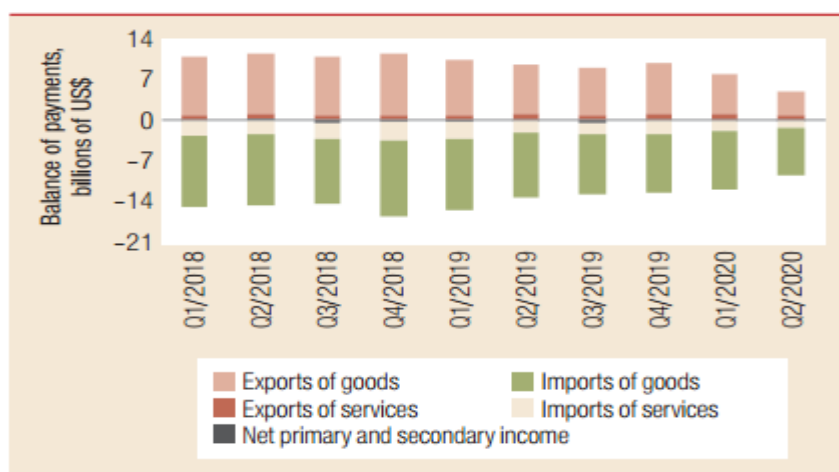


Figure 1. International Trade Collapsed in 2020  
Source: World Bank

## 2.2 Public Finance

The pandemic has led to a significant decline in budget revenues and is expected to lead to increased health and social protection expenditures. According to World Bank projections, hydrocarbon revenues will decline from 13.1 percent of GDP in 2019 to 9.5 percent of GDP in 2020, in line with the contraction in hydrocarbon production and prices. Over the first nine months of 2020, there has been a decline in production by 10.1 percent, and in Sahara Blend prices by 39.4 percent. Direct and indirect tax revenues are also expected to have fallen, in line with economic activity, and the incidence of tax evasion could increase given the economic challenges confronting individuals and businesses. On the other hand, the local currency devaluation against the USD will cushion the fall in hydrocarbon revenues. Revenue financing from transfers of dividends from the BdA was budgeted at 783 million DZD as part of the 2020 Budget Law. Meanwhile, the Government has reduced its estimates of 2020 current and capital expenditures by 5.7 percent through the 2020 Supplementary Finance Law introduced in June 2020. Nonetheless, authorities project that the overall budget deficit will increase significantly in 2020, to 15.5 percent of GDP.

## 2.3 Banking and Liquidity

Notwithstanding the policy response, liquidity in public banks has significantly fallen in the first half of 2020. The fall in public bank liquidity is attributed to the COVID-19 pandemic and the fall in hydrocarbon revenues, leading to a fall in deposits in commercial banks. The six public Algerian banks have increased their financing from the BdA by 404 billion DZD, representing an increase of 36 percent, through open market operations. Among the six public banks—which hold roughly 90 percent of the country's total deposits—four are in a great need of liquidity while private banks are confronted with an excess of liquidity. The monetary base held at the BdA has consequently fallen from 1,100 billion DZD in December 2019 to 840 billion DZD in July 2020, representing a fall of 24 percent.

The tightening of liquidity conditions has led retail depositors to simultaneously seek to withdraw their savings, and put pressure on Algeria Poste, where 35 percent of Algerians hold an account. As a result, Algeria Poste had to impose a ceiling on daily withdrawals.

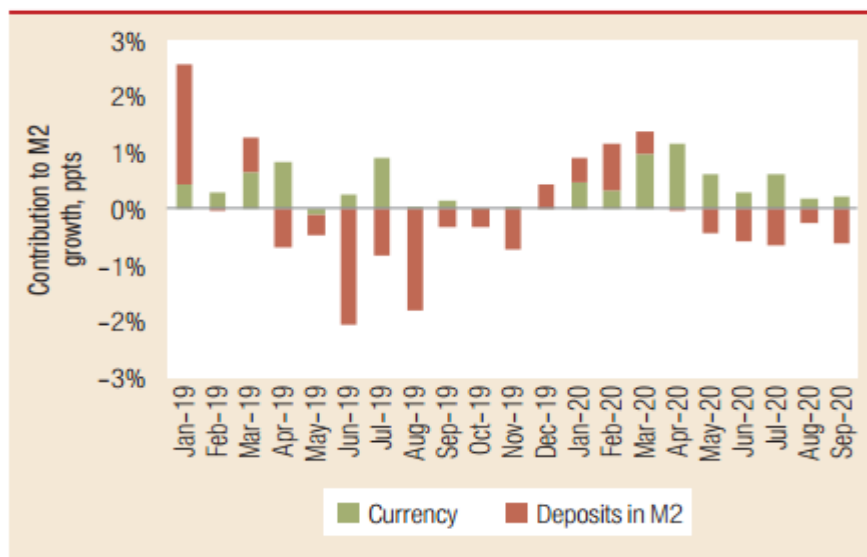


Figure 2. Currency in Circulation Increased as Bank Liquidity Declined  
Source: World Bank

Inflationary pressures on the economy remain contained for now, with diverging trends between the food and non-food national CPI basket. The CPI advanced at an annual rate of 2.0 percent over the first ten months of 2020 relative to the same reference period last year. This is despite the quantitative easing program initiated from September 2017 to March 2019 which injected 4,726 billion DZD in the economy. The food and non-food CPI baskets displayed divergent trends, however. The former advanced by 0.3 percent over the first ten months of 2020 relative to the same reference period last year, in the context of controlled prices for basic food products and efforts by public authorities to limit price increases in fresh products. The latter advanced by 3.3 percent over the same time horizon (World Bank, 2020).

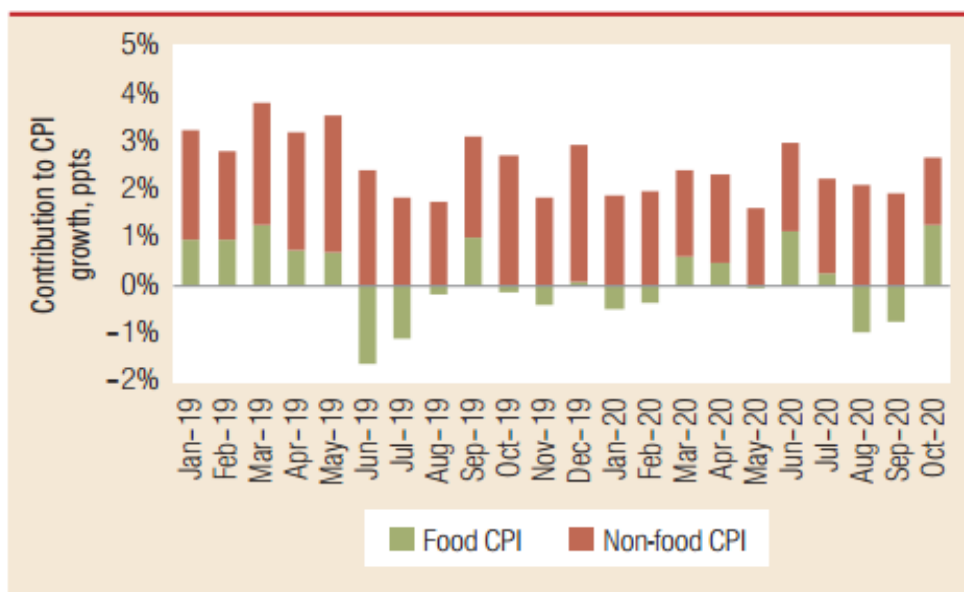


Figure 3. Inflationary Pressures  
Source: World Bank

#### 2.4 Decrease in foreign exchange reserves

At the end of 2020, the forecasts of the 2021 finance Law indicate that Algeria's foreign exchange reserves will be around 42 to 43 billion USD. Over a period of one year, Algeria's foreign exchange reserves experienced a decline of about \$ 20 billion (\$62). Billion dollars by the end of 2019. These large stocks that have been accumulated since the 2000s due to rising fossil fuel prices reached a peak of \$194 billion in 2013. The finance law provides for a reversal of this trend, with the forecast of an increase in foreign exchange reserves by the end of 2021. These reserves have decreased by an average of \$22 billion per year since 2014 and the downward trend in hydrocarbon prices. At \$47.5 billion, an increase of almost \$5 billion per year. Algeria's import reduction strategy, which aims to reduce imports to \$28.2 billion in 2021, is at the origin of this development. According to a statement from the Ministry of Commerce, Algeria's imports experienced an 18% decrease in 2020, reaching an amount of \$ 34.4 billion. However, the objective of reducing imports could be affected by the expected recovery in economic activity (+4% according to the 2021 Finance Law) and the downward trend of the dinar. The current account deficit will decrease to 16.6% of GDP in 2021, against 10.8% of GDP in 2020, according to the IMF (General Directorate of the Treasury, 2020).

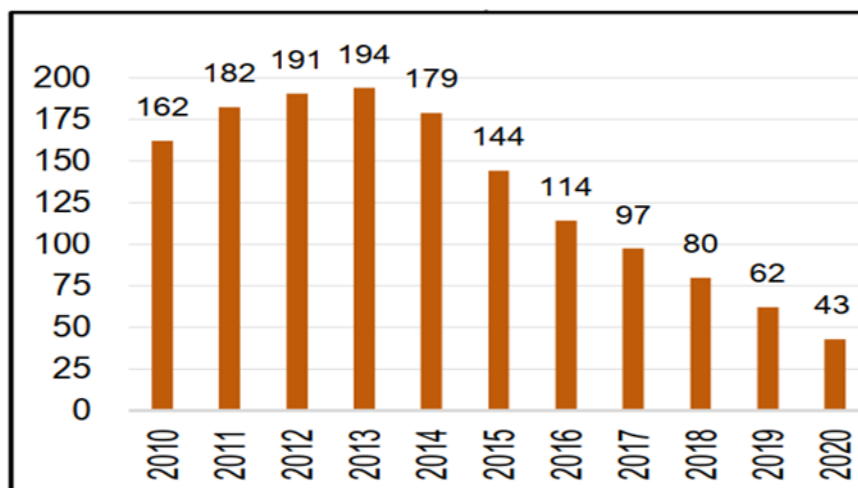


Figure 4. Evolution of Algerian foreign exchange reserves

Source: General Directorate of the Treasury

## 2.5 Debt situation

According to the World Bank, Algeria's public debt increased by 5.8%, from 45.6% of GDP in 2019 to 51.4% in 2020. The World Bank predicts that the country's public debt will increase over the next few years. According to World Bank forecasts, Algeria's debt is expected to increase by 4.7% in 2021 to 56.1% of gross domestic product (GDP), reaching 60.5% in 2022 and 65.3% in 2023. In 2020, it represented 50.8% of GDP, compared to 45.8% in 2019. The government's external debt represents 0.6% of gross domestic product. Algeria's external debt experienced a decrease of 0.4%, from 2.3% of GDP in 2019 to 1.9% in 2020. Even if Algeria could request multilateral or bilateral assistance to finance its large deficit, the external debt will remain low (less than 1% of GDP). The country can also benefit from the financing of the central bank, which ceased its activities in 2019 (Gatti et al., 2021).

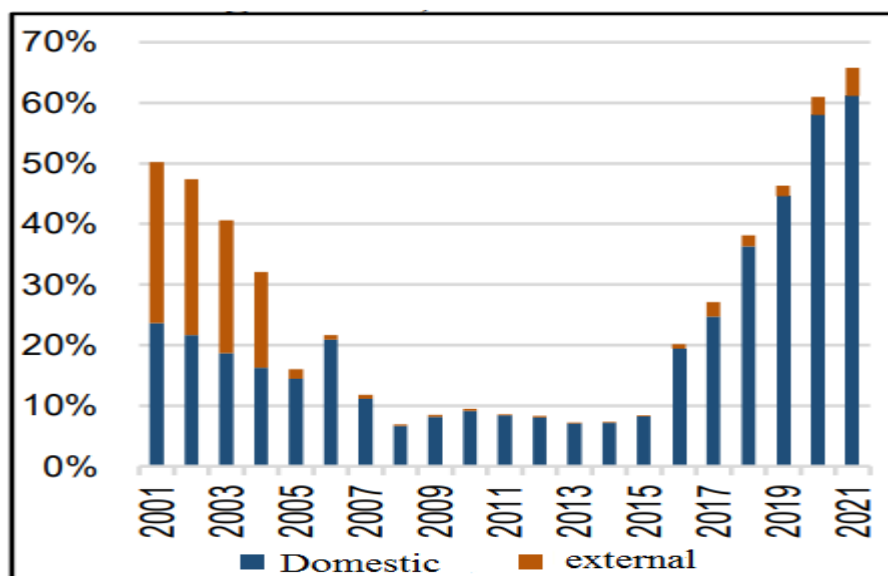


Figure 5. Evolution of Algerian public debt  
Source: General Directorate of the Treasury

### 3. The contribution of Islamic finance tools to financing the Algerian economy during and post-COVID-19."

#### 3.1 Zakat as a financing tool

Zakat in Islam has the following meanings: purification, blessing and is a tax with a tax rate of 2.5% on assets. Zakat is therefore compared to ISF. Any Muslim whose assets exceed the tax threshold (nissab) must pay Zakat. This threshold represents the resources necessary to guarantee the solvency and social needs of Muslims. Zakat cannot be transferred to the construction of mosques, hotels, infrastructure, etc., contrary to what is sometimes mentioned. It can be attributed to:

- ✓ Determined by consensus in favor of direct donations to approved charitable organizations.
- ✓ Transferred to an Islamic bank or to a specific department of a conventional bank.

Zakat is a special resource because the donor, a close or distant member of his family, cannot claim it later. For the poor, it must be used for social and economic purposes (Levy, 2012).

Zakat is widely regarded as a reliable approach to mitigating poverty, in accordance with the teachings of the Holy Quran and Sunnah. It has the potential to serve as a significant Islamic finance instrument in combating the detrimental effects of the COVID-19 pandemic. Zakat is an obligatory monetary contribution made by affluent adherents of Islam, who are compelled to make this payment as a component of their religious obligation. COVID-19-affected individuals, particularly those experiencing poverty, may be offered needed provisions and/or monetary assistance as a kind of relief. Stages 1 and 2 are particularly well suited for providing assistance to impoverished individuals during periods of lockdown,

wherein daily wage laborers and migrant workers face a lack of sustenance for their families (Rabbani et al., 2021).

Zakat, which means "legal alms", could become a crucial element of national and non-governmental emergency aid programs. Donors usually require Zakat to be paid within one year from the date of the donation. Nevertheless, this particular attention to immediate benefits is ideal for dealing with crises. In addition, Zakat donors help both disadvantaged people and those affected by economic unrest, a sector whose demand has increased during the pandemic. Donors also frequently contribute through financial transfers, which can be crucial in an emergency. Personal philanthropy has a huge potential to help with health care, food and other immediate needs. Likewise, companies can use corporate sponsorship to contribute not only in money, but also in goods and expertise (Aamir A R, 2020).

Zakat can also be used to revive the economy during and after the Covid-19 pandemic. The characteristics of this recovery are as follows: Consumption: The redistribution of part of the income from the rich to the poor and the poor encourages investment and increases production to meet the growing demand for goods and services.

Encourage investment: Zakat encourages investment by punishing the concentration of wealth. The production of consumer goods and services for the poor is stimulated by an increase in consumption.

Reduction of unemployment: the activation of the Zakat of the three factors of consumption, investment and production leads to a reduction in unemployment. Zakat creates jobs by creating means of production and investment.

Reduce inflation: In the event of economic overheating, the state is obliged to allocate capital in kind to limit the inflationary trend and extend the expansion period. Distributive policy must distribute cash income in the event of deflation.

Budget balance: Zakat acts as an automatic financial stabilizer during the economic cycle, as people accumulate more and more wealth during periods of economic expansion, and the disbursement of Zakat helps during periods of recession. The amount of Zakat disbursed will be higher during a period of recession because the reserves will be saved during the expansion (Lahjouji, 2020).

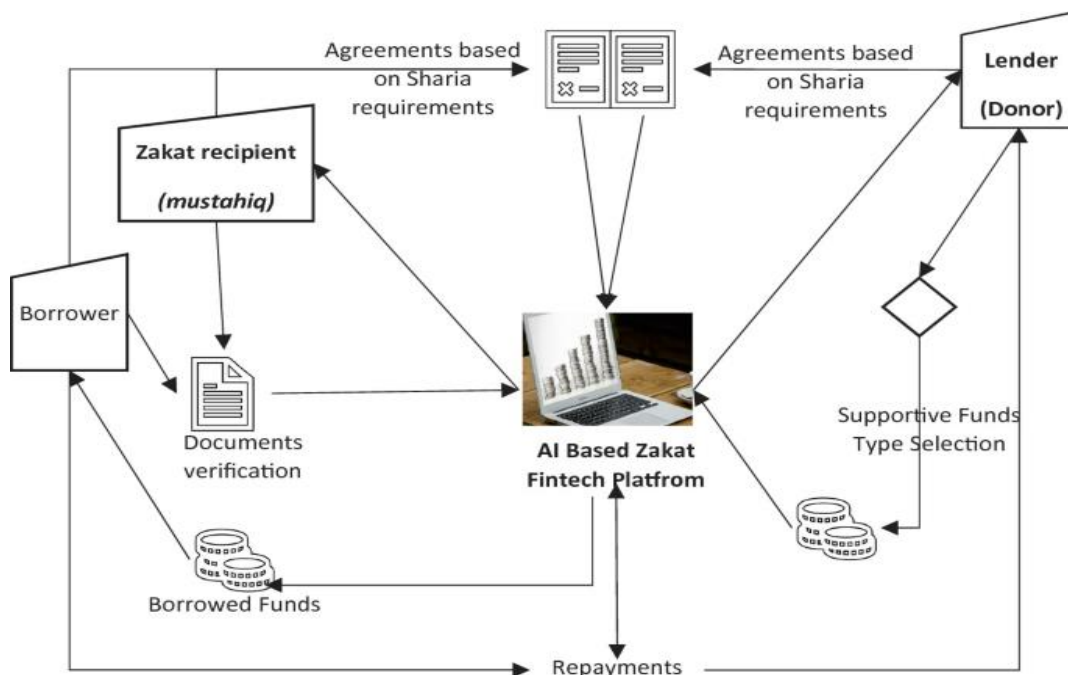


Figure 6. Zakat as a Financing Tool during COVID 19 Pandemic  
Source: (Rabbani et al., 2022)

### 3.2 Qardh Al-Hasan (QH) as a Financing Tool during COVID 19 Pandemic

Qardh Al-Hasan is a non-interest, benevolent loan, or non-margin loan that has been practiced since the era of the Holy Prophet Muhammad peace be upon him. It stands as one of the most elegant financing tools available in Islamic finance. Qardh-Al-Hasan entails a loan given from one party to another without expecting any reward in return. Typically, it serves as a short-term bailout fund.

With the objective of Islamic finance being the alleviation of poverty and the eradication of income inequality, Qardh-Al-Hasan holds significant importance. It is considered one of the most crucial tools in Islamic finance. Qardh-Al-Hasan financing is a traditional method in Islamic finance that remains relevant even in the modern world. If implemented properly, it can aid the SMEs sector in combating the challenges posed by the ongoing pandemic.

Qardh-Al-Hasan refers to lending money to individuals or organizations without charging interest. It is based on the belief that Allah has promised a reward on the Day of Judgment for such acts. The term "Kaseera," meaning "more and more," is frequently used in this context. It signifies that Allah is the ultimate source of abundance, and when Allah begins to reward, there is no limit to it.

The primary objective of Islamic finance is to achieve social justice, eradicate poverty, and promote overall societal welfare. Islamic finance principles are grounded in the aim of assisting the most vulnerable members of society. Qardh-Al-Hasan, along with Zakat and Sadaqah, serves as essential Islamic finance tools for aiding the poor and needy, particularly in times of crisis such as the COVID-

19 pandemic.

As previously explained, COVID-19 has disproportionately affected the poor, and it is incumbent upon Islamic countries and Muslims in other nations to utilize Qardh-Al-Hasan to support those in need. It is the responsibility of society to ensure that the impoverished, including women, are empowered.

The significance of Qardh-Al-Hasan surpasses that of Zakat because there are individuals who may not qualify for Zakat due to their wealth exceeding the minimum limit for eligibility. However, these individuals can still benefit from Qardh-Al-Hasan. With zero borrowing costs, individuals in need can utilize Qardh-Al-Hasan to navigate the challenges posed by COVID-19, restore their financial stability, and later repay the loan.

It has been demonstrated that Qardh-Al-Hasan financing is an effective tool for enhancing the economic activities of the poor and needy. Furthermore, it reinforces social cohesion, cooperation, and harmony. Qardh-Al-Hasan can always be employed to assist the needy and empower them during times of adversity.

One of the key distinctions between Zakat and Qardh-Al-Hasan (QH) is that Zakat cannot be accepted by everyone, as not everyone is entitled to receive Zakat, whereas QH can be accepted by anyone in need of funds, regardless of their financial status. It has been noted that Islamic banks have largely overlooked QH loans as a financing tool for SMEs.

There are several sources of funds that governments and Islamic banks can utilize to provide QH loans to SMEs. With COVID-19 being a temporary phenomenon and many countries already announcing stimulus packages to combat its adversities, funds from these packages can be allocated to finance SMEs through QH loans. This approach can enhance customer satisfaction and loyalty, as SMEs benefit from much-needed financial support.

Banks and Islamic financial institutions can also utilize their capital to finance SMEs during this crisis by offering QH loans, without significantly impacting their liquidity, as these loans are expected to be repaid in due course. Additionally, another potential source of finance for QH loans could be charity amounts received by Islamic banks during Murabaha financing. While these funds are typically earmarked for specific purposes, with client permission, banks can redirect them to help SMEs avoid bankruptcy during the pandemic (Syed et al., 2020).

### **3.3 Cash Waqf in Supporting Economy Recovery during COVID-19**

Cash waqf refers to funds or money gathered by the waqf management institution (nadzir) through the issuance of cash waqf certificates. Alternatively, it can also denote the donation of assets in the form of cash or securities managed by sharia-compliant financial institutions. These waqf funds are subsequently utilized as investments by nazirs in productive ventures, ensuring their adherence to Islamic principles, and the profits generated serve to benefit the community as a

whole (Tho'in & Prastiwi, 2017).

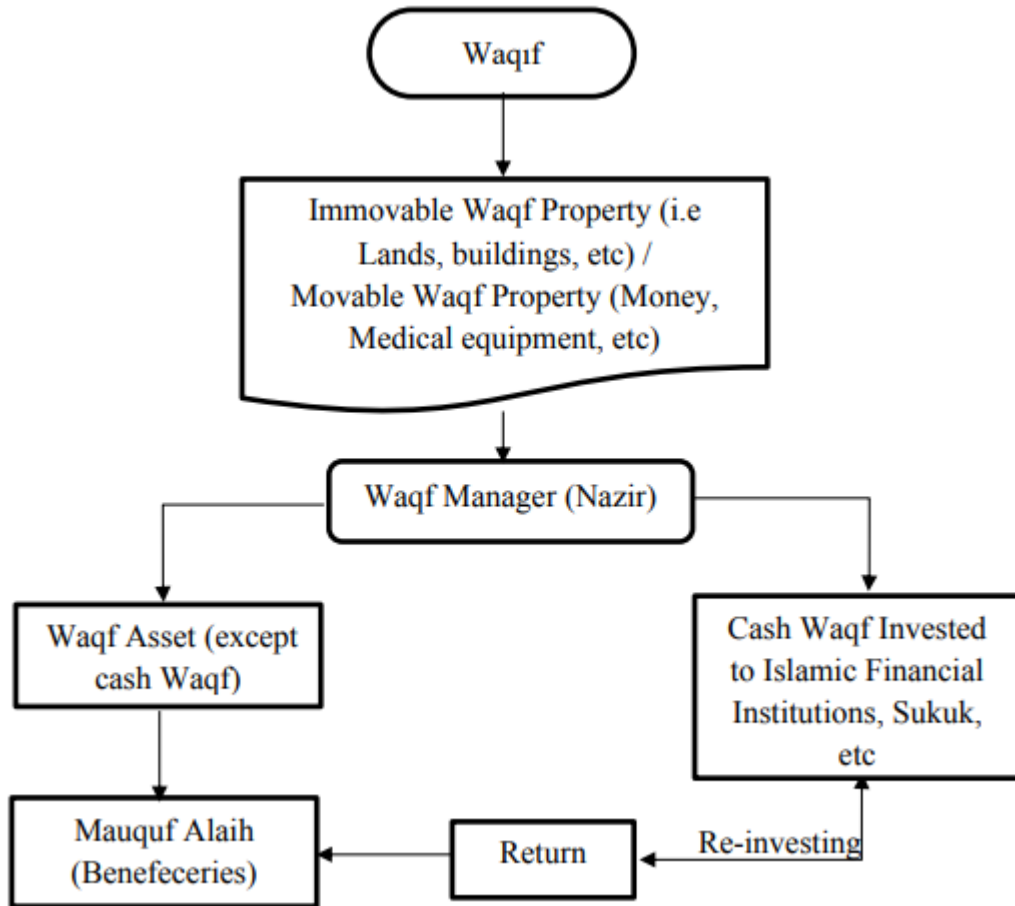


Figure 7. Conceptual Model for Waqf  
Source: (Iskandar et al., 2023)

The suggested form of waqf within the Islamic social finance framework stands out as a potential solution to consider post-Covid-19 pandemic. Numerous researchers have also advocated for Islamic social finance as a means to address the crisis stemming from the pandemic. It is imperative for waqf institutions to fulfill their role effectively, serving as platforms for wealth empowerment and distribution within society.

Waqf serves as a model of philanthropy within Islamic Economics and Finance, contributing to economic recovery amid the Covid-19 pandemic. Various solutions offered by zakat and waqf in the framework of Islamic Social Finance include directing direct cash aid, bolstering cash waqf, promoting productive waqf initiatives, issuing waqf-linked sukuk for infrastructure projects, and providing support to small and medium enterprises through the Qard hasan scheme. Findings from a study further reinforce the argument that instruments like zakat, infaq, and waqf can aid governments in overcoming this crisis (Ascarya, 2021).

While numerous research findings demonstrate the efficacy of waqf in addressing pandemic-related impacts, it's essential to also ensure that waqf funds are prepared for emergencies and disaster readiness. The management of waqf assets with innovative and effective programs must persist, drawing from experiences and lessons learned from current circumstances. The role of the nazir as the steward of waqf properties is crucial in presenting a more efficient program and model of waqf management.

Following the conclusion of the Covid-19 pandemic in various countries by the end of 2022, the economic repercussions will persist within communities, particularly affecting vulnerable groups like small entrepreneurs and the underprivileged. Waqf has played a significant role in pandemic recovery and continues to address a myriad of economic and social challenges stemming from widespread economic disruption and social hardships. One avenue through which waqf can bolster the economy's recovery post-COVID-19 pandemic is by offering financing to small and medium-sized enterprises (SMEs). SMEs typically serve as the backbone of economic advancement in numerous nations. However, they have been severely impacted by the pandemic, experiencing challenges such as cash flow constraints and diminished demand for their goods and services. Waqf funds can be utilized to extend affordable and readily accessible financing to SMEs, aiding them in navigating the economic downturn, sustaining job creation, and fostering continued economic growth (Diniyya, 2019).

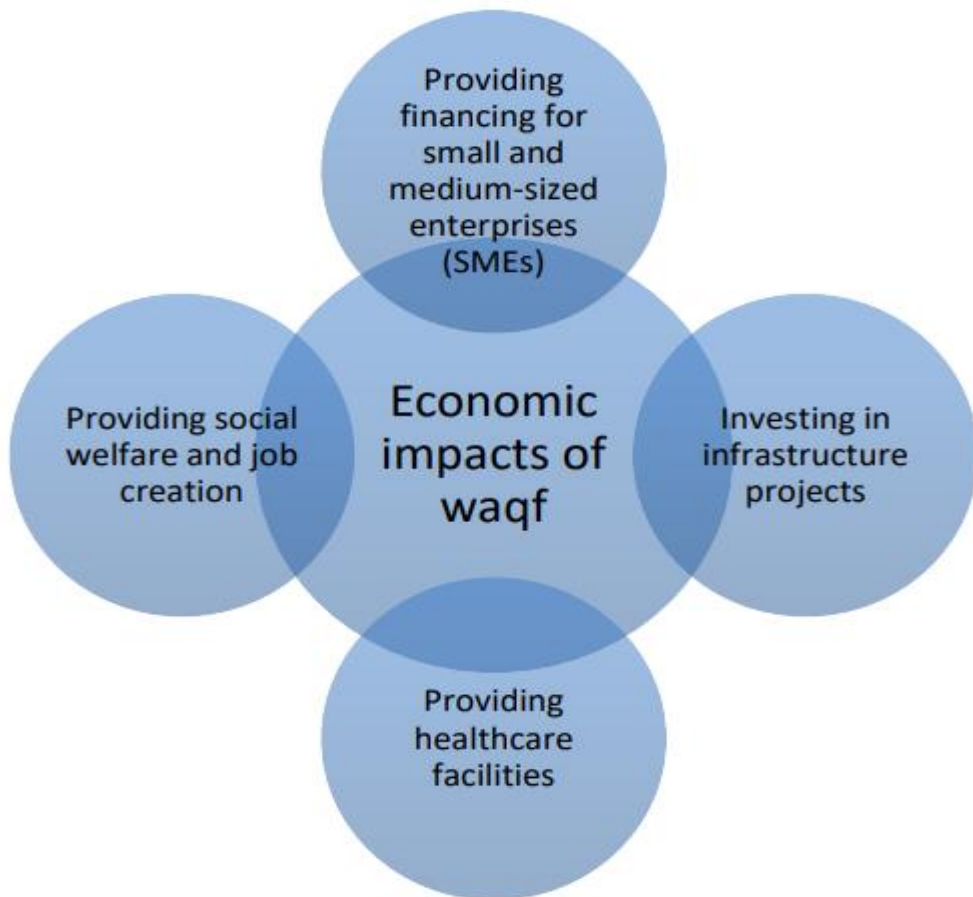


Figure 8. Contribution of Waqf to Economic Recovery Post-Pandemic  
Source: (Iskandar et al., 2023)

The diagram above outlines the diverse ways in which waqf can contribute to rebuilding economies affected by the Covid-19 pandemic. These avenues include providing financial assistance to small and medium-sized enterprises (SMEs), investing in infrastructure projects, establishing healthcare facilities, and promoting initiatives for social welfare and job creation. Waqf contributions can be channeled into projects through cash waqf planning, focusing on endeavors such as income and employment generation, healthcare facilities, and infrastructure development.

The COVID-19 pandemic has underscored the critical importance of infrastructure, particularly in healthcare, education, and digital connectivity sectors. Waqf funds can serve as a financing source for infrastructure initiatives aimed at stimulating economic growth and enhancing societal well-being. These projects may involve the construction and enhancement of hospitals, schools, and broadband networks, among others. By directing waqf funds towards such infrastructure development endeavors, communities can be better equipped to address emerging challenges, improve access to essential services, and facilitate long-term socio-economic progress (Iskandar et al., 2023).

### **3.4 The importance of utilizing Sukuk (Islamic bonds) during the COVID-19 pandemic**

In 2010 the IIFM defined sukuk as a “commercial paper that provides an investor with ownership in an underlying asset.” It is asset-backed trust certificates evidencing ownership of an asset or its usufruct (earnings or fruits). It has a stable income and complies with the principle of Sharia’s. Unlike conventional bonds, sukuk needs to have an underlying tangible asset transaction either in ownership or in a master lease agreement (Safari et al., 2014).

The emergence of the COVID-19 pandemic in 2020 led to unprecedented economic and financial challenges across the world. In this context, sukuk, as Sharia-compliant financing instruments, have played a crucial role in supporting economic stability and recovery.

#### **3.4.1 Sukuk structured upon the Musharaka contract (Equity Partnership, Joint Venture)**

Musharakah defined as an arrangement where two or more parties establish a joint commercial enterprise and all contribute capital as well as labor and management as a general rule. In contrast, investors enter the agreement by paying cash. Therefore, both the investors and the issuer are equity partners in the SPC. However, the investment share in the SPC diminishes over time as the issuer pays installments to the investors to repurchase their respective shares in the asset. These installment payments, plus the issuer’s rental payments for use of the asset (i.e., the asset’s generated income) constitutes the cash flow stream for sukuk holders. In fixed ratio Musharakah sukuk, the cash flow stream for the sukuk holder is only from the income generated from the asset and not from the installment part. The structure of diminishing Musharakah sukuk is depicted in Figure 9.

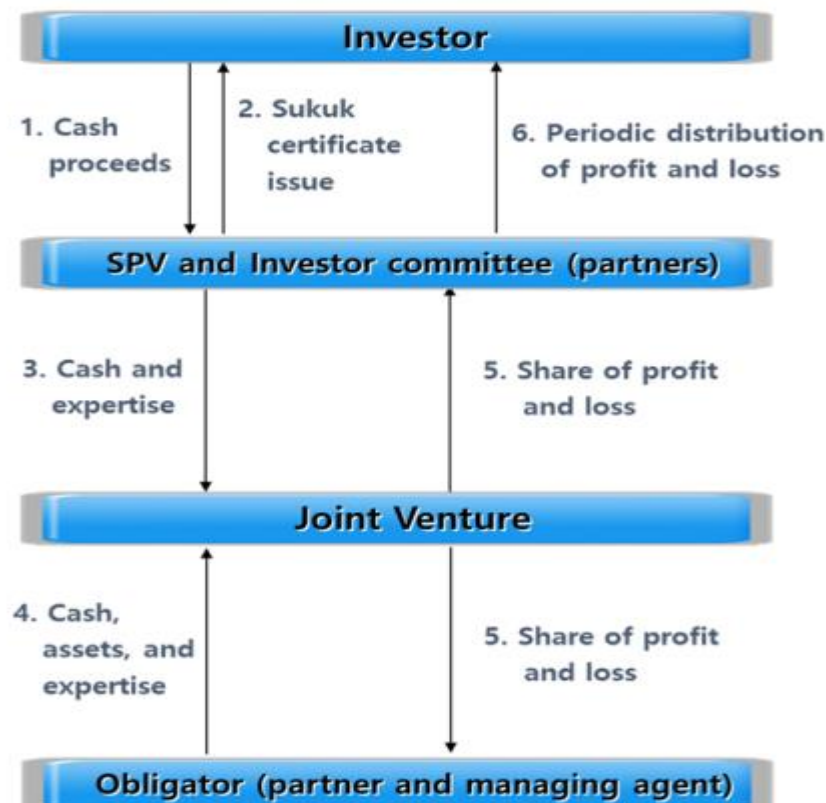


Figure 9. Sukuk structured upon the Musharaka contract  
Source: (Kim, 2023)

Musharaka has the potential to be one of the most effective tools in addressing the economic aftermath of COVID-19. It can be deployed during the fourth stage of the pandemic, namely the post-COVID-19 effects. Musharakah is mainly used to finance real estate construction projects and for financing to small and medium enterprises (SMEs). Islamic banks use the Musharakah instrument in a number of ways and a consecutive partnership is one way in which it can be used. In a consecutive partnership, deposit holders of a bank who keep their deposits for a full financial year become partners in the bank's earnings for that period, irrespective of the employment of their funds during that year. To accomplish this, an adjustment was necessary to overcome accounting challenges related to recognizing profits or losses for each depositor account. Under a Musharakah contract, a joint venture is created as an independent legal entity and Musharakah financing is deemed appropriate for long duration of projects. The financial risk is involved on the part of the entrepreneur and capital contributions may vary from project to project. For instance, the Saudi Hollandi Bank (SHB), based in Saudi Arabia, contributes capital up to 90% in a project and may require representation on the board of a financed joint-venture entity. Musharakah has a wide range of applications in domestic trade, commerce, and agriculture. To enable clients to trade in the local market, the Al Baraka Islamic Bank of Sudan finances on the basis of Musharakah. The bank and its clients form a partnership, and full cost of purchased goods is shared. A special Musharakah

account is opened at the bank. Regarding profit distribution, the bank shares net profit with the client, and surplus profits are divided among the partners of the Musharakah account. But any loss is also shared among the partners in accordance to the capital contributions of each. In addition, the Al Baraka Islamic Bank of Sudan also finances the import of goods under a similar business model as that discussed above. Some other examples of diverse application of financing under Musharakah basis are opening a letter of credit by the Bank Islam Malaysia for its clients to import goods and by the Sudanese Islamic Bank to provide financing for agriculture. Musharakah It is a kind of equity partnership contract that is also widely used for real estate financing. Under this contract, a capital provider, such as a bank, and a customer jointly own the property. However, the ownership held by the bank diminishes with the passage of time as the customer contributes payments. Applications of diminishing Musharakah contracts such as: the purchase of houses, service sector purchases, small business purchases, and commercial and real estate purchases. For example, the Jordan Islamic Bank, based in Jordan, primarily uses diminishing Musharakah to finance the construction of commercial buildings and housing projects like the Irbid commercial market, the municipal college in Jerash, and the hospital in Zerqa. Alrifai pointed out that since Musharakah financing involves high risks and early Islamic banks were not able to manage complex nature of business structures. As a result, early banks took a cautious approach toward using Musharakah. However, this instrument has gained acceptance in contemporary Islamic banking with the availability of well- educated human capital and increasing interest from Islamic bankers in the area of asset securitization (Ashfaq, 2017).

#### **3.4.2 Sukuk structured upon the Mudaraba contract**

Mudarabah is a type of equity based partnership contract that is also known as trust financing, and is one of the core profit and loss sharing contracts in Islamic finance. Mudarabah is described as a passive partnership because one person contributes only capital and takes no part in the management of the business. It is quite similar to the conventional limited partnership contract in which one partner contributes capital and the other contributes management skills, while profits are shared based on an agreed upon ratio.

The basic feature of Mudaraba can be summarized as follows:

- The rabb-ul-mal provides 100% of the capital for the Mudaraba venture.
- The mudarib manages the Mudaraba venture and does not contribute any capital.
- Profits from the Mudaraba are shared between the rabb-ul-mal and mudarib according to a pre-agreed profit-sharing ratio.
- In case of loss, the rab mal bears all losses unless the loss is due to the negligence or misconduct of the mudarib.
- The Mudaraba contract can be restricted (where the rabb-ul-mal imposes restrictions on the mudarib's actions) or unrestricted.
- The Mudaraba is dissolved upon completion of the venture or if any of the contract, conditions are violated.

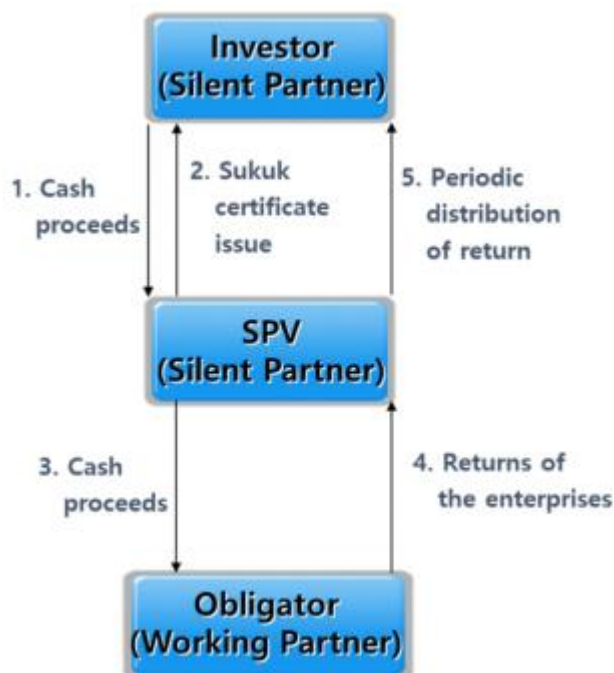


Figure 10. Sukuk structured upon the Mudaraba contract  
Source: (Kim, 2023)

Mudaraba has the potential to be one of the most effective financing tools for providing financial assistance to individuals and small and medium-sized enterprises (SMEs) that have been adversely affected by the COVID-19 pandemic. Mudarabah is a highly recommended Islamic finance profit and loss sharing (PLS) instrument and Islamic banks use it as a mode of financing to “dentists, physicians, engineers, traders Nevertheless, Mudarabah entails high- level risk on the part of a bank because an agent can only be made accountable in the case of negligence. Generally, banks exercise due diligence to mitigate any potential risk before entering into such arrangements. The Mudarabah contract is treated as a short-term partnership in Iran, and banks are advised to engage proactively in cooperative Mudarabah funding. However, commercial institutions are not permitted to extend Mudarabah funding to the private sector for the purpose of imports. Mudarabah is primarily used to fund short duration projects and trade. Therefore, it is mainly used by customers to deposits funds in banks for the purpose of earning profits. Mudarabah contracts have been used mainly for the financing of commerce. It is possible to use such contracts in other areas of the economy such as agriculture, trade, and industry. A Mudarabah contract is used in Islamic finance to fund real estate projects, angel investments, and endowments. In addition, is used to finance the investment projects of companies (Ashfaq, 2017).

### 3.4.3 Sukuk structured upon the Murabaha contract

Murabaha contracts govern the process of buying, purchasing, or importing an item by one party, mainly an Islamic bank, and then reselling it to another party.

The markup is the bank's profit for funding this transaction. The Islamic bank's benefit is generated from the markup on the cost of purchase of the goods, which is agreed upon in advance. Murabahah contracts, which are based on a cost-plus basis, are especially used for foreign trade and working capital financing in circumstances in which banks purchase raw materials, goods, or equipment and sell them to the customer. The ownership of the murabaha asset remains with the Islamic bank until all payments are settled, in contrast to the conventional system, in which the ownership of the assets is immediately transferred to the buyer. Therefore, from modern finance point of view, murabaha is equivalent to an asset backed risky loan and is a popular substitute for interest based conventional trade financing in Islamic banks. To initiate a murabaha, the customer provides the bank with the detailed specification and prices of the goods to be purchased or imported. Having received the application documents, the Islamic bank analyzes and collects the necessary information from the vendors, especially on the price and payment conditions. Then the bank and the customer applying for the murabaha agree on the terms of the deal. Finally, the bank purchases the goods or commodities and resells them to the customer. In order to conduct a murabaha contract, the following requirements should be met:

- Goods and commodities mentioned in the contract must be classified clearly identified according to commonly accepted standards and must exist at the time of the sale.
- The Islamic financier must hold the ownership of the goods at the time of sale to the buyer.
- The cost in terms of net purchase price and the markup must be known at the time of the sale and be declared to the customer. If the bank succeeds in reducing the price by obtaining a discount from the vendor, this discount should be shared with the customer.
- The delivery schedule and the payments must be specified in the contract and cannot be changed during the life of the contract.
- The contract must be based on the sale of a commodity or tangible goods and cannot be based on the sale of money.

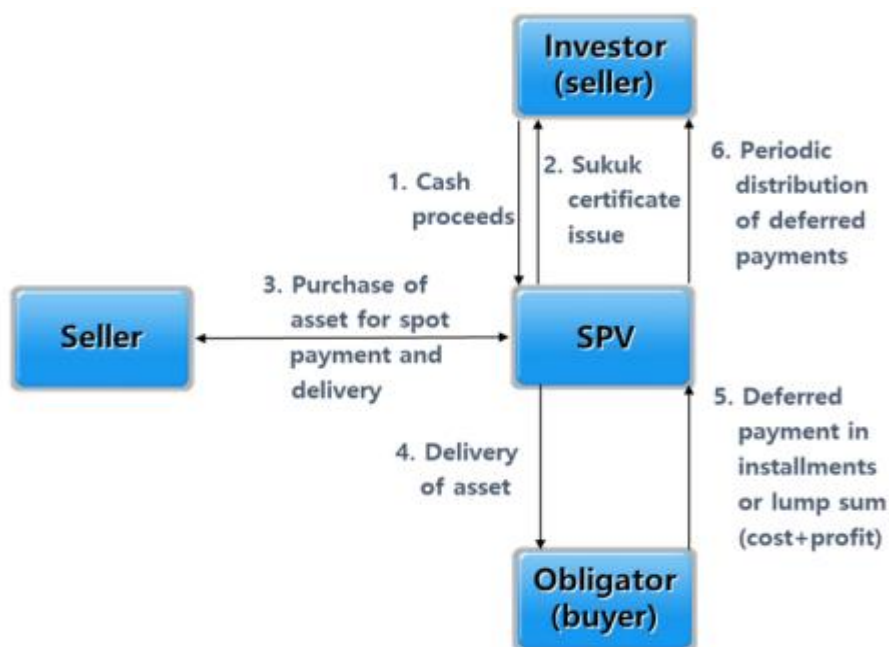


Figure 11. Sukuk structured upon the Murabaha contract  
Source: (Kim, 2023)

Murabaha contracts have the potential to be an effective tool in Islamic finance for combating the economic consequences of the COVID-19 pandemic. Murabaha contracts typically have short-term maturities. Hence, Islamic banks use murabaha for short-term investment and liquidity management, since Islamic banks are still not fully developed for long-term financing. However, murabaha contracts have low returns, leading to an inefficient use of funds and a lower rate of return for Islamic banks. The way murabaha contracts are conducted and practiced contradicts with Shari'ah principles, however, because Islamic banks transfer all costs of insuring murabaha goods against possible damage, destruction, and theft to the murabaha customer. Islamic banks also perform some other actions that are not Shari'ah compliant, such as benchmarking the interest rate to fix the returns on murabaha, assigning higher markups for murabaha contracts with longer periods, charging fines to customers who delay in making their installment payments, and recovering losses from customers who breach their promises to buy the murabaha goods. The murabaha contract is only a contract of appointing the bank as an agent on behalf of the customer in the process of purchasing goods; it does not necessarily involve financing the purchase. In the basic murabaha contract, the customer should pay the cost of the goods and the profit margin immediately after the delivery of the goods. However, the customer can pay by deferred installments or a deferred lump sum without an increase over the original value. In a bai muajjal murabaha sukuk, the issuer pays back the total amount borrowed at a certain time in a predetermined lump sum payment. With a murabaha sukuk, an Islamic bank securitizes its trading transactions with a proportion of the fixed markup providing the return to the sukuk investor, and the bank uses the repayment from its trading client to repay the sukuk holder on termination of the contract (Safari et al., 2014).

### **3.4.4 Sukuk structured upon the Ijarah contract**

Ijarah is an Islamic financing contract where one party (the lessor) purchases an asset and leases it to another party (the lessee) for a specified period of time. The lessee pays the lessor a rent in return for the use of the asset. In Islamic finance, Ijarah can be utilized in two ways. The second type pertains to leasing an asset or property for a fee, similar to hiring the services of an individual for a fee. In conventional finance, leases can be categorized into two types: operating leases, where the right to use the property is obtained, and capital leases, where ownership of the asset is transferred to the lessee at the end of the lease term (Ahmad et al., 2020).

Ijarah is an Islamic financing contract where one party (the lessor) purchases an asset and leases it to another party (the lessee) for a specified period of time. The lessee pays the lessor a rent in return for the use of the asset. Ijarah can be used to finance a wide range of assets, including real estate, vehicles, and equipment. This type of financing can be particularly beneficial for businesses and individuals who need to use an asset but do not want to purchase it outright. Ijarah contracts can be used to provide financial relief to businesses and individuals who are struggling to make lease payments due to the COVID-19 pandemic. For example, a landlord could agree to reduce the rent on a commercial property for a tenant that has been impacted by the pandemic. Alternatively, a bank could provide an Ijarah loan to a business that needs to lease new equipment to adapt to the new economic environment. Ijarah contracts can also be used to finance infrastructure projects that will create jobs and stimulate the economy. For example, a government could provide Ijarah loans to businesses to help them purchase new equipment or expand their operations. In addition, Benefits of Ijarah is:

**Flexibility:** Ijarah contracts can be tailored to meet the specific needs of businesses and individuals.

**Affordability:** Ijarah payments can be lower than traditional loan payments, making it a more affordable option for businesses and individuals. **Shari'ah-compliant:** Ijarah is a Shari'ah-compliant financing tool, which makes it attractive to Muslim investors and businesses. Ijarah has the potential to play a significant role in mitigating the economic impact of COVID-19. It can provide financial relief to businesses and individuals, promote economic recovery, and build resilience for the future. Governments and financial institutions should consider using Ijarah as a tool to support businesses and individuals during this challenging time (Alam et al., 2022).

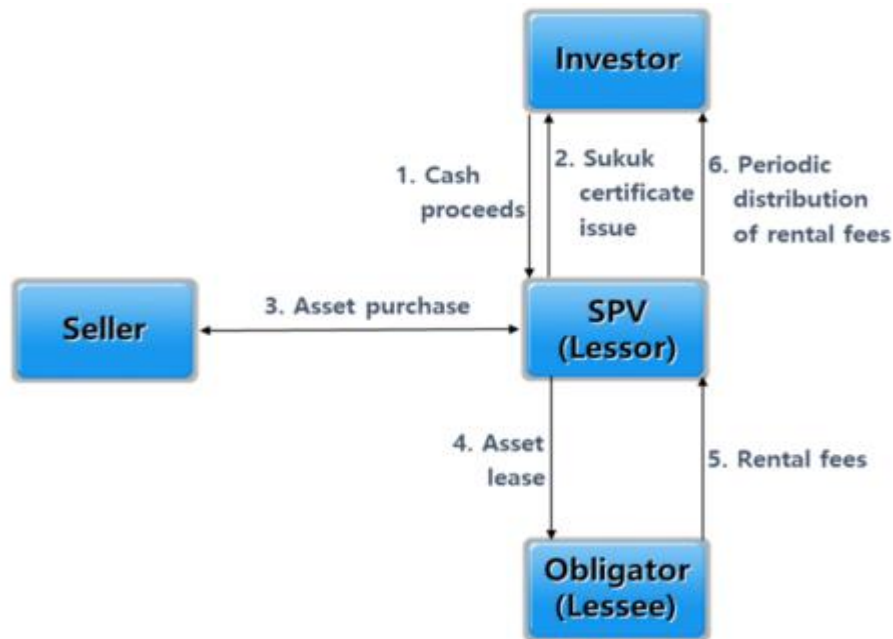


Figure 12. Sukuk structured upon the Ijarah contract  
Source: (Kim, 2023)

### 3.4.5 Sukuk structured upon the Salam contract

Salam a contract in which advance payment is made for goods to be delivered later. The seller undertakes to supply some specific goods to the buyer at a future date in exchange for a price fully paid in advance at the time of contract. According to the normal rules of the Sharia'a, no sale can be affected unless the goods are in existence at the time of the contract. However, Salam forms an exception, given by the Prophet, to the general rule provided the goods are defined and the date of delivery is fixed. It is necessary that the quality of the commodity intended to be purchased is fully specified leaving no ambiguity potentially leading to a dispute. The objects of the Salam sale are goods and cannot be gold, silver or currencies. The latter are regarded as monetary values, the exchange of which is covered under rules of Sarf, that is mutual exchange should be hand-to-hand (spot) immediately. With this latter exception, Salam covers almost everything capable of being definitively described as to quantity, quality and workmanship (Kettell, 2011). The contract must meet the following requirements:

- The commodities and goods have not yet come into existence at the time of the contract.
- The quality and quantity of goods must be known at the time of the contract.
- The delivery schedule and venue must be determined at the time of the contract.
- The buyer must pay the entire price of the goods in advance to the seller at the time of the contract.

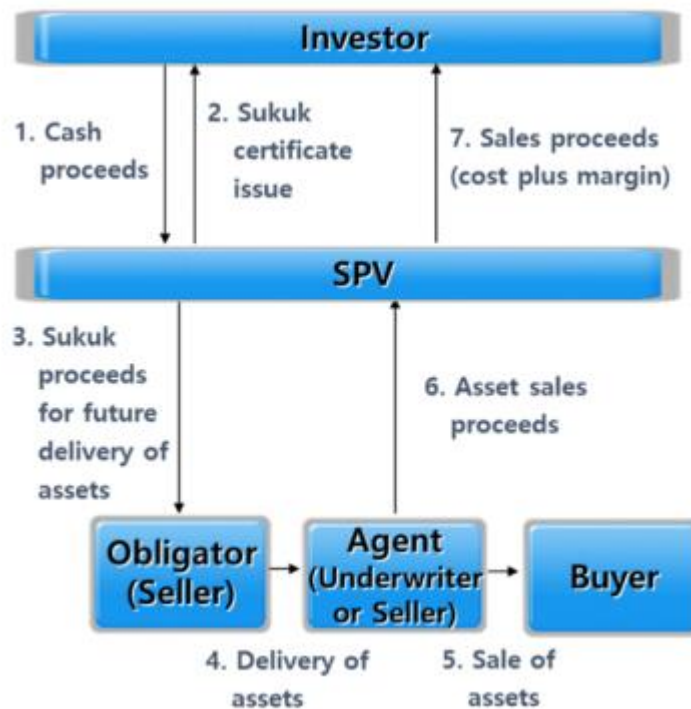


Figure 13. Sukuk structured upon the Salam contract  
Source: (Kim, 2023)

Salam sukuk can play a significant role in mitigating the economic impact of COVID-19. In contemporary economic systems Bay' Salam is used in a number of sectors but most importantly in agriculture. Another important use that has gained momentum in recent years is for providing financing to entrepreneurs in small and medium enterprises (SMEs) to enable the purchase of necessary inputs of production. Therefore, Islamic financial institutions are playing an important role in economic development in various countries. Salam is mostly used to finance fungible manufactured goods and for providing working capital to small traders. On the other hand, Salam contract poses a credit risk to a financier that is difficult to mitigate. One possible situation is that a financier may enter into another Bay' Salam contract with a third party to sell commodities under the same terms and condition as are agreed upon by a seller. Thus, a second contract is made. This is known as a parallel Bay' Salam. It should be differentiated that the financier is not actually selling the commodity and the only purpose in a parallel' Salam is risk management (Ashfaq, 2017).

#### 3.4.6 Sukuk structured upon the Istisna contract

Sukuk al-istisna is the certificate of equal value that is issued for the purpose of mobilizing funds to be used in the production of the goods owned by the certificate holder. The funds raised from subscription are the cost of products and intended products became owned by the certificate issuers, producers (seller/supplier) and subscribers. The certificate holders own the product and

they become entitled to the Sale of a parallel istisna. Sukuk al-istisna is very convenient for financing huge infrastructure projects. Istisna' sukuk are only redeemable at maturity but they can be transferred at face value before that Date. As always with Islamic financial products, the purchasers of the sukuk run the risk of certificates losing value if market price for the produced items falls. This is unlikely in the case of long-term infrastructure products.

As mentioned above, the issuance of istisna' sukuk indicates the right of investors that is sukuk Holders, over the selling price due to deferment of price settlement. This can always be seen in a parallel istisna', which involves two contracting parties in both transactions. In the first istisna' contract, the originator (issuer) agrees to construct istisna' asset and deliver it to the investors on a future date. In return, the price settlement by the investors is payable by lump sum or in phases, according to the stages of completion of the asset. Subsequently, both parties sign separate istisna' agreement, in which the investors agree to construct the asset and deliver it to the originator. In the second istisna' contract, the istisna' sale price, which comprises purchasing price plus profit, will be paid by the originator on a future date. The deferment of price settlement renders the originator indebted to the investors. Pursuant to this, the originator-cum-issuer will issue sukuk as evidence of the originator's responsibility to fulfill its financial obligation to the investors. The issuance is also to represent the investors' ownership over the receivables owed by the originators. The basic structure is illustrated in the Figure 14 (Manzoor et al., 2017).

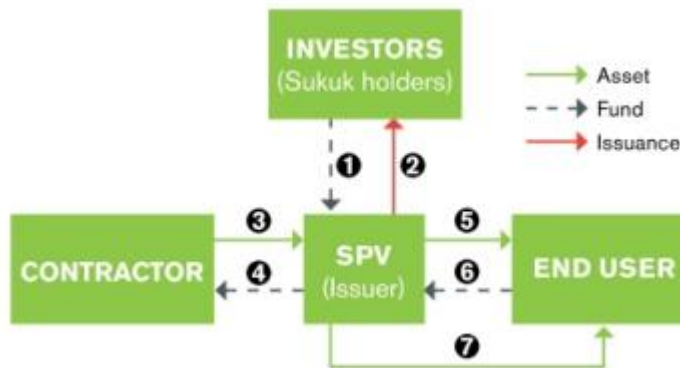


Figure 14. Sukuk structured upon the Istisna contract  
Source: (Manzoor et al., 2017)

Istisna sukuk can play a significant role in alleviating the economic impact of COVID-19. Financing based on an Istisna contract is believed to be the most adaptable form of financing because it offers flexibility in terms of payment method and delivery of goods (Ernst, et al., 2013). Istisnah contracts are useful in a number of industries such as food processing, transportation (aircraft and locomotive), and construction (Said, 2008). Islamic banks also provide financing under Istisnah contracts to support public infrastructure projects including the construction of roads, bridges, industrial complexes, and real estate. In the UK, the ABC International Bank, a subsidiary company of the Arab Banking Corporation Group based in Bahrain, uses Istisnah for construction financing in different cities including Leeds (Ashfaq, 2017).

## Conclusions

The COVID-19 pandemic has had a profound impact on the Algerian economy, exacerbating the existing challenges and highlighting the need for alternative financing solutions. In the aftermath of this global crisis, the exploration of Islamic finance as a viable option for financing the Algerian economy has become increasingly relevant and compelling.

The analysis conducted in this paper has demonstrated the significant potential of Islamic finance to contribute to the economic recovery and long-term development of Algeria in the post-pandemic era. The fundamental principles of Islamic finance, such as the prohibition of interest (riba), the requirement of asset-backing, and the emphasis on profit-and-loss sharing, provide a unique and more equitable approach to financial intermediation. These principles can address some of the limitations and vulnerabilities inherent in the traditional banking system, which has been heavily reliant on debt-based financing.

The adoption of Islamic finance can offer several benefits for the Algerian economy. First, it can diversify the sources of financing available to the government, businesses, and individuals, reducing the overreliance on conventional debt-based instruments and oil revenues. The development of Islamic financial products, such as Sukuk (Islamic bonds), Islamic investment funds, and Shariah-compliant lending facilities, can mobilize domestic and international capital to fund infrastructure projects, small and medium-sized enterprises (SMEs), and strategic economic sectors.

Second, the alignment of Islamic finance with the principles of ethical and socially responsible investing can contribute to financial inclusion and the promotion of sustainable economic development. By catering to the needs of the unbanked population and providing access to financial services that are aligned with Islamic values, Islamic finance can foster greater financial literacy, entrepreneurship, and equitable wealth distribution.

However, the successful integration of Islamic finance into the Algerian financial landscape will require the addressing of several challenges. These include the development of a comprehensive legal and regulatory framework that accommodates Islamic financial instruments and institutions, the strengthening of the institutional capacity and expertise within the financial sector, and the enhancement of financial literacy and awareness among the general public.

In conclusion, the adoption of Islamic finance as an alternative financing mechanism can provide a valuable tool for the Algerian government and policymakers to navigate the post-COVID-19 economic landscape. By leveraging the principles and instruments of Islamic finance, Algeria can diversify its sources of financing, attract new investment, and foster sustainable economic development. The successful implementation of Islamic finance in Algeria can serve as a model for other North African and Muslim-majority countries facing similar economic challenges, contributing to the broader regional and global efforts towards a more inclusive and equitable financial system.

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