



## Digitalization of Islamic Banking

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### ABSTRACT

Digitalization of the Islamic economy can enter various parts of the economy, both macro and micro. Today, digital technology plays a tremendous role in almost every economy. Digitalization is also known as information and communication technology that is used in product packaging and marketing so that information is more easily and quickly distributed. The information is then used to support and accelerate economic growth enabled by digital and information technology. The era of digitalization of information and communication can help both conventional and Islamic economies because information technology has entered into the lives of individuals. Gadget users can now access this technology through mobile applications that have easy-to-understand and downloadable functions. Similarly, in the banking industry, Islamic banking is working with the information technology industry to build a better information system. This application is intended to simplify the entire banking transaction process. The emergence of a digital society is due to the rapid increase and spread of information and communication technology in all sectors, including marketing, economics, finance, services, education, and others. Therefore, digitalization was created to ease user transactions and improve the economy.



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### 1. Introduction

In Indonesia, sharia business activities are now growing rapidly. The rapid advancement of digital technology has also followed the growth. This has brought many countries including Indonesia into the latest technical period commonly referred to as the industrial revolution era. (Asmuni & Arini Indika Arifin, 2023) The industrial revolution brought significant advances in digital technology. It began when advanced computers, intelligent robots, autopilot cars, cell phones, and other industrial equipment still relied heavily on human cognitive power. Rapid change is defined as creative disruption that changes the environment through social interaction and interpersonal relationships. (Muhammad Ismail Sha Maulana et al., 2022) Banking digitalization is a system that uses banking technology to make banking services easier for customers. Banks can increase their customer satisfaction by making digital innovations.

Moreover, banking digitalization allows banks to be closer to people who live far from bank offices. (Tartila, 2022) Various kinds of businesses are starting to shift to follow the developments that occur along with the shift in industrial growth towards digitalization. This shift is one example of the shift of Islamic banking in the current industrial era. (Tartila, 2022) Currently, the rapid development of technology encourages banks to develop digital banking to provide better services. This condition leads to an increase in digital financial service transactions such as mobile payments (m-payments), internet banking, electronic payments (e-money), and mobile banking (m-banking). (Yasin1 et al., 2021) In developing countries such as Indonesia, mobile banking has been introduced before. It was born and developed due to the segmentation of financial institutions that are not managed by the state or the market and are not under the protection, supervision, and regulation of the central bank. Institutionally, the majority of mobile banking is informal financial institutions. One of the characteristics of informal financial institutions is that their role starts from the community to help people and to help themselves in order to develop into intermediary institutions according to the economic path of the community, which are then used as a solution to the difficulties of life in times of crisis. (Gunaepi et al., 2023)

The adoption of digital financial services to access the financial system has benefits as many individuals access the network through computers and mobile phones. Because of this, banks are compelled to meet the needs of their customers as a result of the rapid growth of information technology and changes in consumer behavior. Bank Indonesia also defines FinTech as a new innovation that combines technology and financial services. Therefore, these FinTech ideas are used in the banking industry to generate new ideas that make financial transactions more efficient. (Linton et al., 2020) Overall, fintech improves productivity as well as the economics of payment frameworks and trade exchanges. people's perspectives also influence the use of fintech. In encouraging the use of fintech, people believe that fintech is easy to use, fast, and safe. (Lestari et al., 2023)

In a modern economy, humans need to be able to keep up with technological advances. These realizations and ideas find ways to facilitate human desires to get what they need. (Era et al., 2019) Because various technological and service improvements have been used to increase the number of customers who can utilize Islamic banks. As seen from the various arguments above, the banking industry requires information and communication technology based on the Internet of Things (IoT) to reach customers and achieve effectiveness and efficiency. The potential for Islamic banks to grow and have an impact on the national economy will become more apparent as the use of IoT in Islamic banking increases. Therefore, digital transformation in Islamic banking operations is critical to creating a sustainable financial future. By utilizing innovation and technology, Islamic banking can offer more efficient, effective, and inclusive services to the community, and help the development of Islamic economics and finance in Indonesia. (Farhand, 2020)

## **2. Method**

Based on a knowledge and study of research-related theories from a variety of literatures, library research serves as the foundation for this study. utilizing a range of sources, including books, journals, and many publications. Analytical techniques include descriptive and content analysis (Syamsul & Kuswaya, 2023). Propositions and concepts are supported by a thorough and critical analysis of literature materials sourced from a variety of references.

## **3. Result and Discussion**

In this era of digitalization, the speed of technological development has a significant impact on people's lives. where everything is increasingly moving to the digital era so as to improve the quality of people's lives and the speed of implementation. This digitalization is very important for the banking sector because every customer wants fast, simple, flexible, and

convenient services. The shariah banking industry has undergone a major transformation in terms of technology and information systems in the ever-evolving digital era. The ability of shariah banking to use advanced technology is to meet the demands of increasingly smart and diverse customers. This is essential for the sustainability and growth of the Islamic financial sector (Syamsul & Munir, 2023).

## **Principles of Islamic Banking**

According to the KBBI, "principle" can be defined as the basis or truth on which thinking, acting and other things are based. In addition, principles can be associated with terms such as principle, fundamental, base, foundation, and foundation. (Supriadi & Ismawati, 2020) In the banking sector, especially Islamic banking, progress must be balanced with the implementation and implementation of good corporate governance (GCG). (Parasmono et al., 2022) Banking that provides financial services to the public based on Islamic principles is known as Islamic banking. The prohibition of usury, speculation, and unethical business is the main principle of Islamic banking. (*Perbankan Syariah: Menyelaraskan Sistem Keuangan Dengan Prinsip-Prinsip Ekonomi Syariah*, 2022) According to Law No. 21 of 2008 article 1 paragraph 12, Sharia Banks and Sharia Business Units (UUS) are required to implement effective governance while running their business. This governance must include transparency, responsibility, accountability, professionalism, and fairness. Sharia principles are the basis of Islamic law governing banking activities based on fatwas issued by authorized institutions in the field of sharia (Law No.21, 2008). Thus, the five principles mentioned earlier are the basis of effective Islamic banking governance. Including:

1. First and foremost, (Transparency Principle), which means that Islamic banking must provide an explanation of all relevant information, both financial and non-financial. Where, this financial information includes profit and loss, balance sheet, changes in equity, cash flows and others. Meanwhile, non-financial information includes the basic accounting policies used to prepare financial statements and transactions. In order for Islamic banking to operate professionally and objectively, these principles are very important to apply.
2. The second (Accountability Principle), which discusses how banks are responsible for managing their assets. This idea states that Islamic banks must be able to account for their actions. Therefore, Islamic banking must be managed professionally by considering all parties involved.
3. Third, (Responsibility Principle), states that Islamic banking institutions must comply with applicable regulations.
4. Fourth, (Professional Principles), explains that Islamic banking must act objectively and not be influenced by other parties. To fulfill this principle, Islamic banking must be managed independently, so that no branch dominates and no party can interfere.
5. Fifth, (Principle of Justice or Equality), says that things will be fair and equal when the agreement and the applicable laws and regulations fulfill the rights of the parties involved.

## **Challenges of Islamic Banking in the Digital Age**

The banking sector, including Islamic banking, must undergo digital transformation. The demand for digitalization is increasing, driven by changing public expectations for safe, fast and efficient financial services that can be accessed from the comfort of their own homes. As such, Islamic banking must make digital transformation a top priority and as a way to improve its competitiveness. According to Deden Firmansyah, Director of Sharia Banking Regulation and Licensing at the Financial Services Authority (OJK), Islamic banks must prepare a number of requirements before they can develop digital services, including:

### 1). Human Resources (HR)

Human resources (HR) are a crucial element in the implementation of digital financial innovation. In addition, one of the most raised topics for Islamic banking is human resources. The emergence of Islamic banking in the digital era requires the availability of superior human resources capable of managing the Islamic banking system and ready to meet the needs of rapid technical progress.

### 2). Cyber Security

The existence of IKD in the Islamic banking industry makes cyber security a prominent topic. The increasing epidemic of cybercrime requires Islamic banking to increase knowledge about cyber security. To make decisions Islamic banking must interact with the market economically in order to discover problems and find solutions. Important elements in prevention against cybercrime include security compliance, dedication, finance, management and security.

Financial institutions offering digital or electronic banking services must comply with the regulations of the Financial Services Authority, by implementing risk management, and upholding the concept of prudence, which is in accordance with Article 2 Paragraph 2 POJK No.12/POJK.03/2018.

### 3). Consumer Protection

Of course, consumers and institutions must also be aware of the risks associated with the emergence of digital financial innovation. When digital banking services are provided, protection of customers is recommended as it prevents unwanted events. Customer safety is a top priority for Islamic banking which has a high level of trust in order to gain public trust.

### 4). Lack of financial literacy in society

There is a real gap in society between financial inclusion and financial literacy in the modern digital era. Thus, this is one of the difficulties faced by Islamic banking. In addition to the public's ignorance of the advancement of digital financial technology, the public's ignorance of Islamic banking can also lead to the misconception that Islamic banking is the same as conventional banking. This kind of public sentiment hinders Islamic banking, which seeks to utilize technological advancements to inform the public about Islamic banking through digital advertising.

Islamic banking must implement various strategies to overcome the problems caused by technological advances, including careful selection of human resources to complete the structural components, tightening cybersecurity to protect customer data, and developing more effective ways to overcome public ignorance about banking. (Suganda et al., 2023)

## **The impact of Islamic banking digitalization on the future of sustainable finance in the framework of Islamic sharia values.**

In the financial sector, particularly Islamic banking, there has been great progress due to the use of various technologies. The dual banking system, which is part of the Indonesian Banking Architecture (API), will be used to build the Islamic banking system in Indonesia as part of this change. To create a stable financial future, digital transformation is needed in the Islamic banking information system. Islamic banking can become more inclusive by utilizing innovation and technology. Digital transformation can also help improve people's knowledge of Islamic finance and increase the number of people who can access it. (Parapat et al., 2024)

## **4. Conclusion**

This research provides a clear picture of the digital transformation in Islamic banking information systems and how it impacts the future of finance. First, digital transformation has enabled more people to use Islamic financial services, especially those living in remote areas.

Online and mobile banking has become a powerful tool to increase financial inclusion. Second, the use of data analytics, better system integration, and automation of internal processes are improving operational efficiency. Third, Islamic banking has successfully complied with sharia principles by using technology in supervision and compliance reporting. Fourth, there has been an increase in the types of financial products that can last, such as Islamic bonds that support environmental initiatives and mudharabah-based financing solutions that support social initiatives. Fifth, working with others Islamic banking has utilized fintech companies to keep up with technology trends, accelerate innovation and expand reach. Lastly, supportive legislation is essential to foster the growth of Islamic banking in the digital age. Therefore, this research provides strong guidance and recommendations for Islamic banking to take on digital transformation wisely, maintain sharia principles, and ensure that they contribute to a more inclusive and sustainable financial future.

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