

**MINISTRY OF EDUCATION OF AZERBAIJAN REPUBLIC
AZERBAIJAN STATE UNIVERSITY OF ECONOMICS
INTERNATIONAL GRADUATE AND DOCTORAL CENTER**

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MASTER DISSERTATION

on the topic of

“Economic prospects of Islamic banking in the Republic of Azerbaijan”

Specialty code and name: 060403 - “Finance”

Specialization: “Financial management”

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BAKU - 2018

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ABSTRACT

Today, the interest-free banks widespread not only in Islamic countries but worldwide and rapidly growing, was established in order to meet the financial needs of population, without use of interests and operating according to principles of Islam. The interest-free banks invest funds, collected from the depositors, using interest-free financing principles and distributes profit or loss with the depositors. These enterprises are important because, they win unused funds for economy in the form of investments and evaluate them in the real economy.

In the first chapter of the thesis concept of Islamic economic laws, features of Islamic banking products, Islamic Financial Market Trends, interest-free banking system, the causes for creation of interest-free banks and their main principles, methods for collecting and usage of funds concept of interest and place of interest in Islam were shown. In the second chapter, analysis of the current state of the Azerbaijani banking sector, competitiveness of Azerbaijani banking sector, banking sector development problems have been viewed.

In the last chapter economic perspectives of Islamic Banking application in Azerbaijan have been researched and given experience of foreign countries in the application of Islamic banking. Azerbaijan perspectives of interest-free banks were analyzed and attempted to prepare for action plan for Islamic banking in Azerbaijan.

РЕЗЮМЕ

Сегодня, не только в исламских странах, но и во всем мире, широко распространенный и быстро развивающийся исламский банкинг - это предприятие, основанное на исламских принципах и созданное для удовлетворения финансовых потребностей людей без интереса. Все банки финансируются от вкладчиков без интереса к принципам финансирования и торговли, а прибыль или убыток распределяется между вкладчиками. Для предприятий важно инвестировать в неиспользованные средства в виде инвестиций и рыночной оценки.

В первой главе диссертационного исследования были использованы исламские экономические законы, особенности исламских банковских продуктов, тенденции на исламском финансовом рынке, беспроцентная банковская система, причины создания беспроцентных банков и их основные принципы, место интереса к исламу, сбор и использование средств для банков. Во втором разделе рассматривается текущее состояние банковского сектора Азербайджана, конкурентоспособность банковского сектора Азербайджана и развитие банковского сектора.

В последней главе изучены экономические перспективы применения исламского банкинга, изучен опыт зарубежных стран с применением исламского банкинга. Проанализированы перспективы беспроцентных банков в Азербайджане и предпринята попытка разработать план действий для исламского банкинга в Азербайджане.

XÜLASƏ

Bügün təkcə İslam ölkələrində deyil, bütün dünyada geniş yayılmış və sürətlə inkişaf edən İslam bankçılığı, faiz olmadan da insanların maliyyə ehtiyacını qarşılamaq məqsədi ilə yaradılan və İslami prinsiplərə əsaslanaraq fəaliyyət göstərən müəssisələrdir. Bucür banklar əmanətçilərdən toplanılan vəsaitləri faiz olmadan maliyyələşdirmə prinsipləri ilə ticarət və sənayeyə yönləndirilir, əldə edilən mənfəət və ya zərər isə əmanətçilərlə bölüşdürülür. Bu müəssisələr istifadə olunmayan vəsaitlərin investisiyalar formasında iqtisadiyyata qazandırılması və bazarda qiymətləndirilməsi üçün əhəmiyyətlidir.

Dissertasiya işinin birinci fəslində İslamın iqtisadi qanunları, İslam bankçılıq məhsullarının xüsusiyyətləri, İslam Maliyyə Bazarının trendləri, faizsiz bank sistemi, faizsiz bankların yaranma səbəbləri və onların əsas prinsipləri, İslamda faizin yeri, bank üçün vəsaitlərin toplanması və istifadə üsulları göstərilmişdir. İkinci bölmədə Azərbaycan bank sektorunun mövcud vəziyyətinin təhlili, Azərbaycan bank sektorunun rəqabət qabiliyyəti, bank sektorunun inkişafı problemləri nəzərdən keçirilmişdir.

Son fəsildə İslam bankçılıq tətbiqinin iqtisadi perspektivləri tədqiq edilmiş və İslam bankçılığının tətbiqi ilə xarici ölkələrin təcrübəsi öyrənilmişdir. Azərbaycanda faizsiz bankların perspektivləri təhlil edilmiş və Azərbaycanda İslam bankçılığı üçün fəaliyyət planının hazırlanmağına cəhd göstərilmişdir.

INTRODUCTION

The fact that interest is prohibited in the Islamic religion and the lack of alternative institutions for interest-bearing banks on the other hand would inevitably lead to an investment in the Muslim countries. Despite the fact that the public has the means to ensure the development of the country, the economic needs of the economy are met by external borrowing, and the state has increased political and economic dependence on foreign countries. On the other hand, the money collected from the oil and gas resources of developing Muslim countries was assessed in Europe or America. All of this required the creation of interest-free banks and financial institutions based on Islamic principles.

Non-interest-bearing banks are the financial institutions that are set up to meet the financial needs of the population without the need for interest and the traditional banks performing shopping and trading activities. Although the emergence of the first interest-free banks coincided with the end of the last century, it soon became a significant part of the economies of other countries, not just Muslim countries, but through a long way of development.

Subject level of research. The basis of the Islamic economy and financial system is based on the Islamic religion. The basic principles of the Islamic banking system, such as the absence of interest or the prohibition of the sale of haram products are determined by shar'i. Akgüç Ö., Akın C., Apak S., Özsoy İ., Özulucan A., Pınarız İ., Tunç H., Uslu S., Zeytinoğlu E., Al-Suwailm S., Ayub M. , Hassan MK, Lewis KM, Kettel B., Mehta BK, Visser H., Bidaulet E. A., Haron C. and other foreign researchers. From local authors Mammadov Z.F., Abdullayev AM, Zeynalov ZH, Abdullayev Sh.M. and others have been involved in financial and banking systems, but the interest-free banking system has not been thoroughly studied. The rapid development of the Islamic finance and banking system, the implementation and continuous improvement of new methods of accumulation and use of funds have created new trends for the subject and need to be thoroughly investigated.

The purpose of the research is to compare Islamic banking with the traditional banking system and determine its effectiveness for the Azerbaijani economy.

In order to achieve the research objectives, the following tasks and tasks are important in the research work:

- ✓ To clarify bank and interest concepts,
- ✓ Review the development history of banks and identify their key functions,
- ✓ To analyze the attitude of the Islamic economy towards interest,
- ✓ Determine the reasons, basic principles and functions of interest-free banks,
- ✓ To analyze the methods applied by interest-free banks for the collection and use of funds,
- ✓ To determine the benefits of interest-free banks to the foreign countries
- ✓ Investigate the possibility of applying interest-free banks in Azerbaijan.

Interest-free banks and financial institutions, whose activities are based on Islamic principles, interest-free collection and use of funds are **the object of research**. **The subject of research** is economics based on Islamic principles and financial systems.

Theoretical and practical provisions of domestic and foreign researchers regarding the financial system, bank and interest-free banks constitute **theoretical and methodological basis of the research**. In the research, systematic analysis, analysis, comparative graphics, diagram analysis and surveys have been used.

The books written by researchers and economist scientists on the subject, annual statistical reports of the Republic of Azerbaijan, International Monetary Fund and World Bank related to banking sector, materials published in periodicals, materials of scientific-practical conferences, articles, monographs, state economics, banking and The dissertation and course work on interest-free banking system constitutes **the main database of research**.

The following provisions should be noted, showing the **scientific novelty of the research**:

- The effects of interest-free banks on the foreign countries economy have been investigated,
- Analysis of interest-free banks' opportunities and problems in the Azerbaijani economy.

The practical importance of the work. The results obtained in the dissertation work include the preparation and implementation of various complex field programs and action plans for the development of the Islamic financial system, improving the methods of collection and use of funds used by interest-free banks and financial institutions, the establishment of interest-free banks based on Islamic principles and evaluating the measures, analysis and impacts on the economy.

The theoretical and methodical provisions and practical recommendations, which are studied in the dissertation, are used as educational and methodical aids in the teaching of subjects related to the state economy, the Islamic finance system and the banking sector, conducting research on interest-free banking system, course and dissertation work in higher education institutions It can be done.

The scope of the work. The dissertation consists of the introduction, three chapters, the conclusion and a list of used literature.

CHAPTER 1. İSLAMİC ECONOMIC LAWS

1.1. Scientific bases of Islamic economic laws

Islam is an all-encompassing scientific system covering socio-economic, social-political, legal-ethical, and cultural-ethical rules that regulate and regulate people's lifestyle .The Islamic economy is a term used to express ideas about the possibility of a particular economic development that is defined by Islamic social and moral norms.

This concept, which has been actively promoted in those countries after some African and Asian countries gained independence, has been closely linked to not only developing countries, but also with global economic change projects since the late 70s of the twentieth century, new economic rule ". Planners and project creators propagandize them on the one hand as a cornerstone of a special development path that is fundamentally different from the way of capitalist development. The Islamic economic system is essentially a concept that is characterized by the understanding and specificity of economic processes in the real world based on universal values.

The development of the country and the welfare of the population depend on the acquisition of new investments in the economy. Formation of capital is dependent on the fact that the deposits of the population are directed to the subjects, who need investments in the economy. In the economy, the transfer of such resources is carried out by the financial system. Banks are the basis of the country's economy and financial system. Banks are the lenders who lend money to their depositors at the expense of their depositors, with interest payments. The interest is considered to be the bank's interest and is distributed to depositors.

The main aim of interest-free banks is to support the economy in accordance with the economic principles adopted by Islam. Non-interest-bearing banks operate to create a market where there is no interest, the risk is distributed, and commodity products that do not contradict Islamic rules.

Interest in Islamic literature is "riba". Riba expresses meanings of meanness and increase. Interest is not a profit-making activity, it is a measure of reducing revenue, reducing revenue. As interest rates lead to the growth of non-working goods, it results in the burden of the wealthy people who are not engaged in any business.

The foundation of the Islamic economy, where interest is forbidden, is based on the Quran. The basic principles of the Islamic economy are as follows:

- Interest is prohibited in any form,
- Money is not merchandise trade, it is a tool of change, storage, and measurement,
- Risk sharing is fundamental. In a trading and partnership-based system, the risk is shared between the parties,
- Artificial intervention in the market and black market understanding are unacceptable,
- Uncertainty transactions are forbidden. Games or speculations that are highly risky are prohibited,
- The rules set out in the treaties must be observed. However, the rules set out in the treaty should not contradict Islamic principles,
- The terms of the contract, the obligations and obligations of the parties should be known,
- Simply acting on Islamic laws and products may be subject to financial activity. For example, alcoholic beverages or gambling are prohibited,
- Social justice should be taken into account.

The Islamic economy does not accept the advance payment of interest in the form of interest. Because it is unclear whether the lending money would bring profit due to the dynamic and volatile economic conditions. As a result, there is a difference between the fixed interest rate and profit. This difference can create difficulties for either the debtor or the lender.

It is impossible to speak of the welfare of the society in the interest society. That is, when the society is divided into borrowers and lenders, the other side is facing a difficulty while enjoying a party at any interest rate. The negative features

of interest and the ban on Islam have led to the creation of interest-free banks and resulted in the implementation of activities in this direction.

Non-interest-bearing banks are the financial institutions that perform traditional banking activities to meet their financial needs without the need for interest in their shopping and trading activities. Although interest-free banks are theoretically similar among other banks, there are also contradictions. Thus, the traditional banking system is fundamentally capitalized and it is impossible for such banks to operate without interest. However, the framework of interest-free banks is defined according to religious orders and prohibitions. Free banks make collections and donations on a partnership basis. Therefore, instead of pre-determined interest, the entity receives or transfers a gain or loss on the basis of the results of the operation.

In general, six primary activities of interest-free Islamic banks are distinguished:

- Prepaid credit interest payments are prohibited,
- Sharing profits and losses is the basis of the Islamic system,
- It is unacceptable to make money through money,
- Speculation actions are prohibited,
- Only Sharia-approved contracts are accepted,
- Contracts are sacred.

Non-interest-bearing banks, in contrast to traditional banks, are not intended to earn direct profits from nominal activities, but are a system that provides funds for trade and production activities or directly engages these activities. As a result, the interest-free banking system's profit is not the interest earned by selling money, but rather the proceeds from economic activities. The point of interest of the non-interest-bearing banks is the form of money, rather than money.

The main features that distinguish interest-free banks from traditional banks are:

- The capital of interest-free banks is gold, received from individuals and legal entities. Lenders may borrow money if they wish,

- An interest-free bank is not a profit-making entity. The Bank operates in the form of a joint-stock company with funds or funds. Those who use banking services earn profit or loss,
- Interest-free banking plays a role as a broker in loan and debt management. Risk does not take directly to itself,
- Increases and decreases caused by non-bank-related causes of the Bank's deposit are the name of the owner,
- The Bank's loan-related decisions are based on predetermined criteria; the ability of bank managers to make their own decisions is minimized as far as possible,
- Loans to interest-free banks are credited as loans, and loans are credited to individuals or individuals. Both legal and economic risks of the loan are under the guarantee of the interest-free bank.

Factors causing the creation of interest-free banks can be grouped under four main headings: *religious, economic, political and social reasons*.

Religious Reasons: The reason for the origin of interest-free banks was the ban on interest in Islam.

Economic Reasons: The first economic reasons for the emergence of interest-free banks are the oil revenues derived from the oil fields of Islamic countries in the 1970s. As the oil revenues of OPEC (Oil Exporting Countries) countries increased, oil revenues from the exporting countries increased considerably. The revenues of these countries were directed to the Western countries and did not help the development of Islamic countries. On the contrary, it had a negative impact. On the other hand, despite some natural resources of some Islamic countries, it lagged behind its growth due to lack of capital. The purpose of directing capital from relatively developed Islamic countries to capital suffering from capital deficit was the basis for the creation of interest-free banks.

Political Reasons: Political causes for widespread non-interest-free banking systems in some Islamic countries have also been influential. In Pakistan and Iran, the desire for a government based on religious grounds, and Saudi Arabia's desire to keep wealthier managers under the control of oil revenues can be

illustrated by the political reasons that are effective in building interest-free banks. On the other hand, one of the objectives of interest-free banks such as the Islamic Development Bank is to enhance cooperation between Islamic countries and form a strong political will at the international level.

Social reasons: The society consists of individuals. Since economic opportunities and living standards are not equal, economic classes are created in different characteristics. The well-being of the society depends on the establishment of good relations among individuals belonging to these economic classes, the continuation and elimination of the gap between economic classes. At this point, interest-free banks help capitalize the economy and increase employment through the production factors. Interest-free banks play an indispensable role in ensuring the integrity of social justice and society.

The basis of interest-free banks is four basic principles:

Lack of interest

The primary feature of non-interest-bearing banks is that interest is not paid. That is, the bank does not pay interest for the proceeds. Instead of using funds, they do not receive interest from their customers. The Islamic economy admits that capital is a production factor and its cost. However, it does not accept the predetermined return of the production factor, ie interest. In other words, making money with money is forbidden.

Being related to trade

In Islam, the haraam of interest, trading, and profits make it lawful for banks to engage in commercial activities with customers. Since trade in money is forbidden, commodity trade is necessary to make a profit.

Being related to capital

Under Islamic law, the capitalist may be able to cover the gains that it ends up with the experience, opinion, and labor of an entrepreneur. Capital gains are predetermined in proportion to the extent to which profits are to be deducted. But the amount of profits is uncertain. As a result of the activities, profits can be as damaged as possible.

Investment Ethics Compliance

The Islamic Bank does not finance the activities prohibited by the sale of alcoholic beverages, pork and other haram products. At the same time, religiously speaking, if the Muslim community falls short of food, clothing, health or education, production and marketing of luxury products or activities are not accepted morally. Investments should be carried out outside the scope of the Islamic religion. Islamic investment: should not be harmful to the environment, be charitable, provide community participation, and respect human values.

Given these principles, the following features of interest-free participation banks are identified:

Interest-free banks are based on profit share: As a result:

- Profits and losses operate on the basis of dividends on banks and customers.
- Cash loans are not issued.
- Money is not earned through money.
- Production, investment and trade. The collected funds are used for the benefit of society.
- Both bank and customer are at risk.
- Higher interest rates are not received from clients who are unable to pay in due time.

Risk sharing: The person who invests in the Bank becomes an investor. The Parties shall accept the risk of reducing the profits or losses arising from trade and production activities. Profit or loss between the borrower and the lender should be fairly distributed.

Speculative activities are forbidden: Spreading activities in the economy do not generate added value for society. Those who earn money from speculation can cause uneven distribution of existing wealth. The main purpose of the application of this feature in interest-free banks is to prevent the vulnerability of the economically vulnerable parties.

Elimination of uncertainty and the importance of the contract: Interest-free banks pay attention to the fact that contracts are transparent. All duties,

responsibilities, responsibilities and rights must be clearly stated in the contract, without any doubt. The provisions of the treaty that may lead to uncertainty should not be included, all items must be stated in strict terms.

Non-permitted Areas: Participating banks pay attention to the fact that the areas to be funded are not forbidden by Islam. For example, there is no loan for fields and activities such as production and sale of alcoholic beverages, gambling establishments.

Community and Personal Benefit Balancing: Traditional banks offer cash loans to customers who can repay debt. In most cases, it is not followed where this loan will be used. Non-interest-bearing banks are exposed to economic activities, as well as the consequences. For the benefit of the community, the benefits of the society and the rights of the individual for the benefit of society are not allowed. This is under the control of which areas the funds are directed to.

Accumulated funds feature: From the moment the account is opened for deposits in a traditional banking system, the customer knows in advance how much money he will get at the end of the term. This payment does not depend on earnings or losses using bank deposits. Non-interest-bearing banks do not guarantee the payment will be made at the end of the term.

Profit and loss sharing: In traditional banks, profit or loss from deposits is only within the interest of the bank. In interest-free banks, the gain or loss is distributed to holders of the account.

Effects of Use of Funds on the Economy: Traditionally, banks have limited impact on the economy because they are lending money. Some of these loans are accessible to the real economy, while others may be inefficient. Non-interest-bearing banks use different methods to convert funds into investment.

Peculiarity of the used funds: Since the interest-free banks do not have a loan, the client's funds should be directed to the economy. For this reason interest-free banks can not buy before the purchase. The price determined by the client banks does not change depending on the change in the economic conditions. At the same time, owners of funds can not buy their money at the bank before the time.

Traditional banks can increase interest rates or recall used funds. For this reason, some trade and industry companies face difficulties. There is no such risk in the participating banks.

Participation Banks' source costs: In traditional banks, profitability depends on interest earned on loans and interest paid to depositors. In treasury banks, the cost of accumulated funds on balance sheet is determined based on earnings from the funds used. Therefore, there is no fixed cost beforehand.

After reviewing the basic principles and characteristics of Islamic banks, the main functions that interest banks should be able to achieve their goals and objectives.

These features include:

1. Crediting function

The interest-free bank performs the function of lending to assessing the deposits of individuals and legal entities. The funds owned by these persons are allocated to the persons or organizations in need. After payment of the debt by a person or organization using the loan, the value corresponding to the credit value and period used by the bank is used for those who benefit from banking services. Such lending is carried out without interest, and the bank does not receive any rewards for this activity.

2. Liquidation function for partnership documents.

One of the major activities of the bankless banks regulates the share certificates of the invoices, carries out the functions of preparation of share certificates contracts and provision of necessary guarantees. The Bank puts out the shares of the investing company, and saves its depositors to form a share capital for the firm. Stocks are deposited in the bank, so the Bank does not earn any profit or loss from these activities.

3. General service function.

Interest-free banks provide support to individuals and businesses by providing services such as accounting, marketing or legal support in addition to

banking services. Non-interest-bearing banks, together with funds or non-profit organizations, serve as a general service.

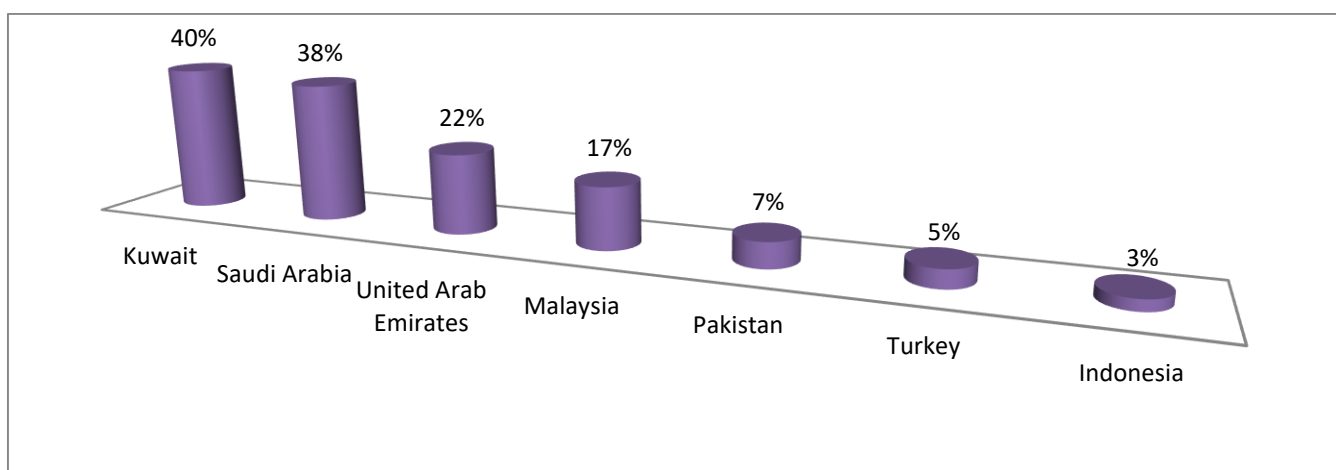
Implementing this function increases the effectiveness of economic activity. Because these services are costly and costly for small and medium-sized enterprises. Small entrepreneurs can not carry out these activities due to financial problems, resulting in difficult competition with large enterprises and monopoly conditions.

Recent fluctuations in the financial markets have given rise to new tools and applications in this area. The lack of investment in emerging and underdeveloped countries as the biggest obstacle to greater profits from international trade has led these countries to adopt new methods. There is a need to create interest-free banks to ensure that the developing countries are using oil and gas reserves in their own countries or in other Muslim countries instead of evaluating their money in European or American countries.

In recent years (2013-2016 years), the share of interest-free banks in the entire banking system has also grown dramatically.

Figure 1.1.

Share of interest-free banks in the banking system (2013-2016 years)



The fact that interest is prohibited in Islam and the lack of alternatives to interest-bearing banks on the other hand has prompted Muslim countries to buy foreign currency, gold, or property, which in turn would have resulted in capital exploitation. This has resulted in the nation's ability to meet its capital needs

through external borrowing and to depend on the country's political and economic dependence, even though it has funds to support the development of the country.

The foundations of the modern Islamic conception of Islam were established in the second half of the twentieth century. This concept was actually isolated from existing Western economic thought and oriented to Islamic rules. It is known that the religion of Islam is indivisible and social characteristic is characteristic.

Islamic finance has been shaped on a balanced interconnection system of state, co-operative and specific division, with the idea of "acquired property", which is the basis of the new socio-economic structure, based on the relevant economic concept. In this financial concept, traditional Muslim taxes have been declared part of the Islamic economic system. By banning the interest rate, Islamic banks, including the unified Islamic Development Bank, have been set up as interest-free economists, as a regulator of economic life.

The initial growth of Islamic finance was reflected in the 1973-1974 and 1979-1980s due to the huge positive balance of oil exports from Islamic countries. Despite the decline in oil revenues in the coming years, the expansion of Islamic finance has gained momentum on other factors. This perspective first focused on the establishment of socio-political systems based on Islamic principles, and subsequently the Arab oil dollars directed towards the shares of the West Components and the banks' deposits. In such a situation Middle Eastern countries have become more portfolios.

At present, the economic principles of Islam at the state level are implemented in several countries. Meanwhile, progressive leadership belongs to Malaysia. Traditional Muslim societies respond in two ways to the contemporary superiority of the West's technological strength and economy. The first aspect is to achieve development by exceeding the distance by adapting to modern Western culture. This direction can be characterized as the transformation of Islam. The second aspect is fundamental or Islamist. His goal is not to master the culture of the West, but to strengthen its development on the basis of Islamic culture. In the

modern era, Islamic countries prefer to expand research into higher technology spheres. Modern financial investments focus on progressive technologies in these countries' direct investment networks, including the military sphere.

The expanding capacity of the scientific and technical progress, which is based on Islamic finance in the Islamic world, and the development of information technology on the other hand, provide a new angle of modern civilization in those countries. Some Western politicians note that the concept of jihad, which is one of the key aspects of the Islamic perspective, has developed in the IT industry. From this point of view they point to the fact that modern e-jihadism is one of the most important manifestations of Islamic economic expansion in the cyber space of e-jihad. The appropriate approach does not exclude mysterious moments and prudent grounds. It's not a disadvantage that six of 10 countries belonging to the highest rates of information technology are Middle Eastern states. The UAE is the second in the list, leaving behind only China. As can be seen, Islamic finance has the potential to fulfill the function of virtual jihad and to join Sharia laws .

1.2. Features of Islamic banking products.

The business success of an individual in Islamic finance is rewarded. Islamic finance and its confessional banking system differ in this aspect. The organization of Islamic business, which holds the principles of justice in the economic sphere, is a form of joint venture partnership. In this area, the Islamic banking system is in the forefront of the business and provides an effective business venture. The first typical banks operating on the principles of Islamic principles were established in the US in the 60s and 70s of the last century and expanded their geography rapidly to the Islamic economies - first to Egypt, then to the Middle East and other Asian countries.

The Islamic bank's secularism created conditions for the establishment of a magnificent Islamic Development Bank in 1973. The bank, which was established at the conference of financial ministers of Muslim countries, was fully functional in 1975. Its purposes are based on the Islamic law, which speaks for the benefit of the social and economic development of the Muslim world. The IDB has a capital of 55 member countries. Participation in cooperation here is primarily based on ICO (Islamic Conference Organization) membership. Currency of IDB, located in the headquarters of Jeddah, Saudi Arabia, is the currency of the bank's conventional currency. An IDB dinar is now worth about \$ 1.33. IDB's official language is Arabic. However, English and French are used as a working language. In a number of IDB countries, regional offices and numerous related branches are functioning. At present, modern Islamic banks carry out all traditional banking operations. However, non-interest-bearing, non-speculative Islamic banks are distinguished by superior operating systems.

Because the interest-free banks are set up to earn and use assets efficiently for the non-bank population due to interest rates in the financial sector, interest-free banks can be analyzed in two ways: aggregation and use of funds.

Methods of accumulation of funds

In addition to the bank's own capital, funds collected from the population are used to finance interest-free banking operations.

Islamic Bank opens three types of interest-free accounts for its customers:

Current account -Accounts are opened by owners in order to meet their need for business or trading needs and to be ready for circulation. These accounts resemble termless savings accounts used in traditional banks.

Private current accounts are non-investing accounts, and are non-term accounts that hold funds. It is mainly used for short-term cash needs, money transfer or repayment needs. No minimum limit for opening an account. It can be opened either locally or in foreign currency.

Owners of personal accounts can open accounts for caution or for future use. Current account holders are mostly low-income or simply people with payroll income.

Here the bank is allowed to pay for customer service. In the course of inflation, the bank provides compensation to depositors in the nominal interest rate;

Investment Account (Participation Accounts) - Investments funds spent on various transactions in accordance with the terms and conditions of the Bank's profits and losses;

Accounts are opened in the participating banks for the purpose of earning income for those who do not invest in their own funds because they are forbidden by the interest rate but who are unable to make a profit on their own. Account holders earn a portion of the Bank's profit and loss on the amount and timing of the deposited money. These accounts will be opened in accordance with a business partnership agreement.

Deposits are credited to the real sector under the terms of the profit or loss sharing contract, with the term specified in profit or loss. It is also unclear how much profit a person will be able to earn at the end of the term because the profits will be affected by the projects financed in the system.

The feature of the affiliate account is that, unlike traditional banks, there is no relationship between the depositors and the bank, but the relationship of profit

and loss. Returns the nominal value of the principal debt as it does not have any fixed income before the interest rate or ratio is determined.

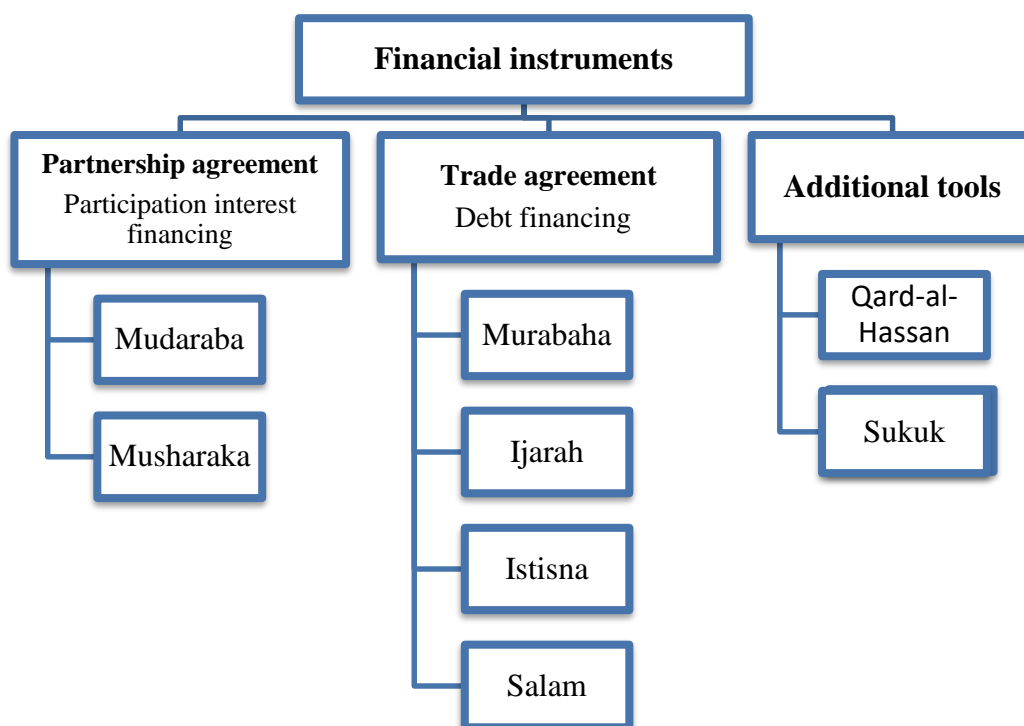
Credit account - Long-term or short-term loans are provided to the needy entrepreneurs. Deposits wealthy Muslim funds and provides credit to their peers. The Bank, in its turn, ensures that the funds are repaid to the depositor within the agreed time.

Methods of using funds

Non-interest-bearing banks use funds earned by depositors to invest in those who need them. This use is sometimes accomplished by way of partnership, sometimes through sale or lease of the necessary goods. Financial instruments of Islamic banks can be classified as follows:

Figure 1.2.

The main financial instruments of Islamic banks



1. *Musharaka* - Arabic partnership, partnership, joint project with the bank and the entrepreneur. The interest aspect of this transaction is reflected in the distribution of profits in terms of shares, efforts and skills. The loss is divided between the participants in proportion to their share of funding. Here, the bank acts as a real participant at all stages of the transaction and its results, and also carries out its

functions of financing and control. Partnerships are not required to be Muslim in the deal type. However, the fact that one of the parties is Muslim is conditioned by its leadership in its oversight functions. Here, each partner has a dual function, which is also a trust and a ground. Investing funds must be free, its dimensions and affiliation must be transparent and not to create conflicts in the process of liquidation and liquidation.

The distribution of earnings may not be equal, as it is not necessary to equally distribute equity in Musharaka. Profit sharing may not be proportional to the capital ratio and is determined by agreement between the parties. During the distribution of profits, each capital can receive any amount of money from its share based on the division of interest. If there is no profit, the amount withdrawn from the partnership is deducted from its capital. The loss of the loss is determined by the ratio of equity capital to total capital.

2. *Mudaraba*- Reliability Orientation Financing. In the conciliation agreement, which deals with the basic principles of Muslim farming, the essence is that it is a party that offers capital, and a divorce party manages it by investing in business. Here, profits are distributed in return for pre-determined propots.

After signing a contract with the bank, the bank submits the capital (the contract) to the customer at his discretion. An outside bank can not interfere with the activities of the project owner. However, preventive measures can be taken if unexpected loss of risk as a result of unplanned and irregular work. The Bank may request checks for accounts at any time and may request from the customer all official and unofficial documents.

Necessary measures are taken to eliminate or minimize the possibility of loss. For this purpose, the project is thoroughly analyzed when a client who needs an investment requests a bank. If the project is considered to be profitable, the bank will decide to make a deposit to the client. Also, if the expected amount of revenue is not available, the customer's future funding requirements may not be met. The resulting earnings are also distributed between the bank and the customer at a predetermined rate. If the project activity is at the forefront, the bank will

receive all capital. Neither the bank nor the customer benefits. In case of loss, the bank is welcomed. The customer will lose the work and time spent on the project implementation. However, if the customer has a fault in the occurrence of the damage, the customer pays the loss.

3. *Murabaha* - is based on the principle of trading in commercial and commercial operations in Arabic. Here, the bank takes the full amount of profit by taking over the whole risk and financing its commercial operations. Specifically, commodities are purchased in this operating cycle and re-realized by adding appropriate interest rates. The difference is profit.

A non-interest-free bank that is in need of a commodity, but does not have the necessary funds, will apply for the purchase of this item. An interest-free bank buys this item and adds a profit to it and sells it to customers on time basis. Profit share used in this method is similar to interest. Interest-free banks take interest rates when determining their profit share in murals.

To carry out the *Murabaha* transaction, the product must be physically available and sold after purchase of the bank. Client's application or instruction should be recorded in writing, since the customer who wishes to buy the goods may be exposed to the risk of subsequent risk. The timely sale of the goods can be either single-time or in installments. The bank may request a guarantee from the customer for payment.

A number of Islamic scholars state that this operation is contrary to Islamic principles of non-interest. Even in the final decisions of the Pakistani Supreme Court, the sale of the past sale of the crochet and the bai-maker has been declared as non-Muslim financial transactions since the rebate elements were sold.

4. *Ijarah* - Participating banks are called "leasing" in traditional banks, and leaseholds to their customers. Rental is used as a source of more medium and long-term financing. At least two parties are involved in the lease: the owner of the leased property is the lessee who rents the rent and rents. The amount and dates of the rent are determined based on the tenant's and the tenant's needs and the characteristics of the goods. Rental activities are carried out on a contractual basis

between the lessor and the lessee. The contract must specify the payment and the term of the rent. The ownership of the goods belongs to the affiliate bank that owns the property. The rent period can be between 5 and 15 years.

Application of the lease is carried out in two forms. In the first method, the Participating Bank rents a company or person in need of the customer to buy the goods he / she needs. After the contract expires, the seller rents or rents goods from another customer. In the second method, it does not withdraw from the customer after the contract expires, and sells it to the customer for a symbolic payment. For this reason, second-rate rentals are higher. The reason for this is the fact that the participation banks take into consideration the rent of the goods, as well as the value of the goods given to the customer at the end of the term. This method is sometimes referred to as "lease and power."

5. Salam- The type of contract is the type of contract that provides the buyer with a pre-paid repayment payment and the subsequent delivery of the goods at a later date. Salam's sale was used in the early years of Islam. Farmers were selling seeds that were sown by seed, meeting seed and fertilizer needs. Salmon sales contract can be applied not only to wheat, barley or other agricultural products, but to all kinds of products, goods and equipment.

There are two main features of the sale of plums. Firstly, the full amount of the product price must be paid in advance in advance. Secondly, after the harvest, the delivery should be carried out by the buyer.

It can be both a natural person (investor) and a bank as buyer in the sale of plums. After the goods have been delivered to the buyer, the investor may sell it to the third party. The Bank may agree with another customer in advance of the shipment of products to minimize the risk of price risk. At the same time, the bank may minimize the risk by selling alternative cash.

6. Istisna- is the type of contract that provides for the sale of any commodity, such as usury, at an agreed price at a later date. However, the construction or production of the goods subject to the contract is distinguished from the point of view of the fact that advance payment is not a prerequisite for the payment and is possible to

pay. The Istisna contract is widely used for construction projects. Islamic banks exclude high technology products from the Istisna method - aircraft, ship, construction and so on. for their production.

The agreed price may be increased unilaterally. However, construction projects may take a long time and may change in the course of the project. It is therefore permitted to modify the previously agreed price with the consent of each of the parties. Istisnas are not needed in advance. Price can be paid in installments or after completion of the project.

The application of the Istisna method in the Islamic bank is at the following stages:

- The customer applies to the bank with a new production, construction or property acquisition project. Project quality, price, composition and so on. information is provided to the bank. The Bank analyzes the project from an economic and religious point of view.
- The Bank agrees with the implementation of the project.
- The Bank signs a contract with the manufacturer or construction company.
- Based on the contract, the results of the work shall be provided to the bank or to the customer.

7. *Card-al-Hassan* - interest-free loan. The Bank grants to the physical person and to the institution a loan repayment date. These funds are separated from special funds of banks. Such banks even provide government with interest-free loans for the implementation of relevant projects.

Non-interest-bearing banks, in addition to the methods provided, also provide loans for non-profit purposes. These loans are considered as social loans. This method lends interest-free loans to those who need it. Debt settlement is within the period determined by the agreement of both parties. Interest-free banks do not generate any income as a result of this transaction.

Although no repayment percentage is applied to the debt of *Karz-i Hasen*, the customer can make additional money from the debt, as a gift, in return for the debt.

These funds can be used to finance smaller industrial projects, such as marriage, illness, education, or some extraordinary events. Funds are met by current accounts or interest-bearing banks' personal investment. If the customer falls into an unbearable situation, the bank's social funds are welcomed.

8. *Sukuk*- Certificates that represent a proportional undivided ownership right in tangible assets, or a pool of tangible assets and other types of assets. These assets could be in a specific project or specific investment activity that is Shari'ah-compliant. Sukuk is based on a particular asset or property, other than those other documents. Real estate is the sale of real estate through movable property through lease certificates. As a result of the action, the certificate holders share in the certificate earnings from real estate.

Sukuk has the following characteristics:

- Transparent and clear understanding of the rights and obligations,
- Revenue from securities should be related to the purpose of financing,
- Securities should be supported by real assets, ie they should not just be a piece of paper,
- The availability of the second-hand securities market will provide liquidity for Sukuk,
- The sukuk owner provides regular earnings, but also the ability to earn awards.

Tavarruck

The transaction to sell cash to another person in cash from one person in order to obtain a cash is called a "commodity sale". Interest-free banks are trying to balance the liquidity and flow of cash flows required by the customer to meet their financial obligations.

Tavarruck is carried out in the following stages:

- Interest-free bank or interest-free bank deposits a specific amount based on a contract between them, ordering to buy any item on its own behalf and at its expense.
- The second bank receives the same item on behalf and at the expense of the client who is the customer.

- The second bank requires the customer to sell the item on behalf of his client, and sell it to the customer at a certain rate of profit.
- Then, the second bank keeps or sells the property it owns. There is no trade relationship between the banks, only the term borrowed.
- When the time expires, the first bank pays the second debt.

Another application form of the Tavarruck is related to meeting individual financial requirements of customers. Individual trades implemented by some participating banks resemble traditional bank system applications. Especially, customers who want to avoid interest rates are used to meet urgent financial needs such as treatment, education and marriage.

Individual exercises are as follows:

- First of all, the bank receives a customer's credit that is equivalent to the amount of loan that a customer or product needs.
- It then sells the purchased item to the customer on a regular basis by adding a certain profit share. The activities carried out here are the Murabaha operation.
- The customer disposes of the property sold to the bank or sells the product to the bank.
- Sales amount is added to the customer's account. The difference between the selling price and the bank's current sales price is the profit of the bank.

There are various opinions about whether the Tavarruck transaction is in line with Islamic rules. Some scholars think that there is no problem in religion, while others hold the same rate. Nevertheless, it is natural for a person who has a cash problem to earn money by selling cash from an interest-free loan market.

Other Usage Methods

In addition to the implementation of the Islamic banking, new methods of use of funds have also been started. One of them is the honey system. This method can mainly be used for interest-free loans in accordance with the amount and timing of the customer's investment in the bank. For example, a client who deposits a bank for \$ 5,000 for a dollar of \$ 1,000 will earn an interest-free loan of \$ 5,000 for a year.

Participating banks offer non-cash loans to their clients, along with cash loans. The basis of these services is a letter of credit (letter of credit) and letter of guarantee.

The letter of credit is a loan issued by a correspondent bank to a bank's third party under the instruction of the customer. It is widely used in import and export payments. If the terms of the letter of credit are met, the bank undertakes to pay for the goods and services.

The letter of credit is as follows:

- The importer and exporter who will carry out international trade comes to an agreement. It is determined that the payment will be made by way of credit.
- The Consignee applies to the bank and instructs the exporter to open the letter of credit.
- Letter of credit (bank of importer) sends an application to correspondent bank (exporter's bank).
- Correspondent bank provides information about the issuance of a letter of credit to the exporter.
- The exporter sends the products according to the terms of the letter of credit and all necessary documents are submitted to the correspondent bank.
- Correspondent bank documents submit to the importing bank.
- After receiving the analysis of the documents by the consumer, the correspondent bank makes payments.
- The Consumer is using the bank credit card and does not receive a loan from the customer. The value of the goods from the addressee during the period of the letter of credit.
- Importers submit bank documents to the importer for the goods to be imported.

The letter of credit gives the exporter the opportunity to pay, to protect against the exchange risk, and to provide financial support. The Consignee receives the advantage of obtaining a loan and obtaining a product in accordance with any conditions.

Guarantee letters are widely used in the banking system. The basis of this service is to provide the Bank with the amount payable in case of failure to perform a job within the framework of the trust. The Bank guarantees its customers to use their trustworthy letter of guarantee. The client can also implement projects requiring substantial funding by using this letter.

In addition, Islamic banks try to execute insurance activities indefinitely. Insurance activity in traditional banks is called **takaful** in interest-free banks. This application is based on the likelihood that people will face the risks of life-threatening. Quarantine provides customers with financial resources to meet the challenges that may arise as a result of emergence of risks.

Non-interest-bearing financial institutions offer almost all of the modern banking services offered by traditional banks to their customers in various ways. The key focus of interest-free financial institutions is to simplify the client's business and to formulate a financial system based on religious grounds.

It should be emphasized, however, that the Islamic banking service format is not naïve. Here, the applicant is required to have certain managerial skills and competency requirements in his area, his financial standing, his solvency, and, in some cases, mortgages are also required. Islamic banking and credit operations and operating activities are not limited to the above mentioned forms and mechanisms. While this system of operations is the essence of Islamic profiles, their circle of activities improves according to the Shari'ah practice and adapted to new realities. Such approach banks are inevitable for the economy to go to the real sector of the economy and to manage relevant projects.

1.3. Islamic Financial Market Trends.

Islamic finance has grown rapidly over the past decade, and its banking segment has become systemically important in a dozen countries in a wide range of regions. Islamic finance is projected to continue to expand in response to economic growth in countries with large and relatively unbanked Muslim populations. It is also fueled by the large savings accumulated by many oil-exporting countries that are seeking to invest in Shari'ah-compliant financial products.

Shariah Supervisory Board (SSB) plays an important role in the Islamic banking system, and it has an important impact on their performance and stability. The study concentrates on the banking system and on the SSBs as an important part of it. The study aims at showing the impact of the SSBs on the Islamic bank stability. It also reveals the importance to be Independent department in the implementation of its decisions. The study concluded that SSBs is a significant department in the Islamic bank like the other departments. The interference of it decision-making and management could adversely affect for the Islamic bank.

According to the definition of Shariah Supervisory Boards (SSBs), There is no standard definition for the SSB, and it has many definitions. As Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), the SSBs are an independent body of scholars and specialists in transactions by adding another member to the specialists in the field of Islamic financial institutions who is familiar with the field of Islamic transactions. The member of SSB is responsible for the follow-up the tasks and the validity of the implemented transactions in the IB and to find legitimate solutions to the irregularities. The SSBs also responsible for following up, examining, analyzing activities, business, behaviors, and operations that carried out by the several Islamic Financial Institutions (IFIs), to ensure that they are in accordance with the rules and principles of Shariah. The SSBs using the appropriate legitimate tools and methods, with the indication of mistakes and corrections, at the same time, finds a legitimate alternative.

The SSB has the task of Fatwa by answering to the questions and queries, whether those inquiries are from the employees of the IB or the customers, also participating in the preparation of drafts of decrees, decisions and orders presented by the bank, in addition preparing explanatory notes thereto. As AAOIFI (2010), the main functions of SSB are:

- Directing, reviewing and supervises the institutions activities to ensure Shariah compliance.
- Shariah advice and guidelines.
- Shariah approval on products and services.
- The functions of final review.

Shariah compliance defines as failure to comply with the Shariah rules and principles determined by the Shariah board of the IBs and IFIs or what IFSB is called "IIFS", or the relevant body in the jurisdiction in which they operate. Shariah compliance in Islamic banking also defines as a phenomenon that ensures that the banks underlying financial products are in accordance with the rules and laws defined by the Shariah that is revealed upon the last Prophet of Islam Muhammad. The compliance requirements must be pervasively infused throughout the organization as well as in their products and activities, This becomes realistic by the adequate system and controls, such as Shariah Board/Advisor . According to the IFSB (2014), the reputation risk may arise from inappropriate business conduct and significant failures in Shariah compliant. This proves the extent of risk that can be exposed the Islamic bank, as a result of the intervene in the SSBs decisions.

The researcher concluded that the possibility of interference in the work of SSBs may lead the Islamic bank into errors and irregularities legitimacy, which may lead to the adverse consequences to the Islamic bank. The presence of legitimate mistakes, and the failure to comply the adopted principles in the application of some of the contracts, therefore the Islamic bank may expose to the non-compliance risk, which is one of the important risks in Islamic banks. The researcher concluded that, the exposure of this type of risks, i.e. Non-compliance

risk may lead to the reputation risk, which could impact on the financial stability of the Islamic bank.

The growing reach of Islamic finance promises a number of possible benefits. For example, it is often argued that Islamic finance is inherently less prone to crisis because its risk-sharing feature reduces leverage and encourages better risk management on the part of both financial institutions and their customers. It is also argued that Islamic finance is more stable than conventional finance, because: (1) Islamic finance involves prohibitions against speculation; (2) financing is asset-based and thus fully collateralized; and (3) it is founded on strong ethical precepts. Moreover, Islamic financial institutions (IFIs) are considered to be a good platform for increasing access to financial inclusion, including access to finance for SMEs, thereby supporting growth and economic development.

Nonetheless, Islamic finance faces a number of challenges. For example, despite the efforts of Islamic finance standard setters, in many countries the industry is governed by a regulatory and supervisory framework developed for conventional finance. Therefore, it does not fully take account of the special nature of Islamic finance. The industry is still largely a nascent one, lacking economies of scale, and operating in an environment where legal and tax rules, financial infrastructure, and access to financial safety nets and central bank liquidity are either absent or, if available, do not appropriately take into account the special characteristics of Islamic finance

The Islamic equity markets suffered in 2015 and during most of 2016 from volatility-inducing political uncertainties, slow growth, depressed oil prices and volatile commodity prices. However, the unexpected election outcome in the US triggered a stock market rally in November and December, Islamic equity and fixed income funds benefited from the good performance of the Islamic equity indices and the increased *sukuk* yields. Positive results of Islamic commodity funds are mainly due to an increase of the oil price at the end of the year. Although the returns were positive in 2016, the resilience of Islamic funds cannot be taken

for granted as most of them lack scale: 73% of the Islamic funds have less than USD 25 million AuM (Assets Under Management) while the average size of conventional funds is USD 394 million AuM(Assets Under Management).

The *sukuk* market, however, reversed its earlier decline and *sukuk* outstanding expanded by 6.06% to close at USD 318.5 billion as at end-2016 [2015: USD 300.3 billion]. The widening budget deficits in key developing and energyexporting countries encouraged a flurry of fund-raising issuances in 2016 – including debut sovereign *sukuk* issuances by Jordan and Togo – and the sector expanded its overall market share in the IFSI to 16.8% [SR2016: 15.5%]. The gross contributions in the *takāful* sector have also increased by 13.1% to close at USD 25.1 billion as at end-2015 [2014: USD 22.2 billion] and represented 1.3% of the global IFSI [SR2016: 1.2%]. As an indicative comparison and in US Dollar terms, the international debt securities outstanding in global markets⁵ increased by 2.65% (between end-2015 and 1H2016); and the premiums in the global insurance industry grew by 3.8% in 2015⁶.

Figure 3.1.

Breakdown of IFSI by Sector and by Region (USD billion, 2016*)

Region	Islamic Banking	Şukūk Outstanding	Islamic Funds Assets	Takāful Contributions	Total
Asia	218.6	182.7	19.8	4.4	425.5
GCC	650.8	115.2	23.4	11.7	801.1
MENA (ex-GCC)	540.5	16.6	0.2	8.4	565.7
Africa (ex-North Africa)	26.6	1.9	1.5	0.6	30.6
Others	56.9	2.1	11.2	–	70.2
Total	1,493.40	318.5	56.1	25.1	1,893.10

* Data for şukūk outstanding and Islamic funds is for full-year 2016; data for Islamic banking is for the six months ended June 2016 (1H2016); data for takāful is as at end-2015.

Source: Islamic Financial Services Board (IFSB) Secretariat Workings

The growth of IB, in particular, outperformed conventional banking over the past decade. IB has thus increased its penetration in many countries, crossing the threshold of 22.5 percent as a share of banking system assets in 10 countries (Iran and Sudan with a full-fledged Islamic financial sector, Bangladesh, Brunei, Kuwait, Malaysia, Qatar, Saudi Arabia, the United Arab Emirates, and Yemen) (Islamic Financial Services Board 2017). IB represents about 1¼ percent of global banking assets. During the recent global financial crisis, Islamic banks were less exposed to

the toxic assets that contaminated the conventional banking world, but suffered from second-round effects, notably through the real estate slump.

Figure 3.2.

Islamic Banking Share in Total Banking Assets by Jurisdiction

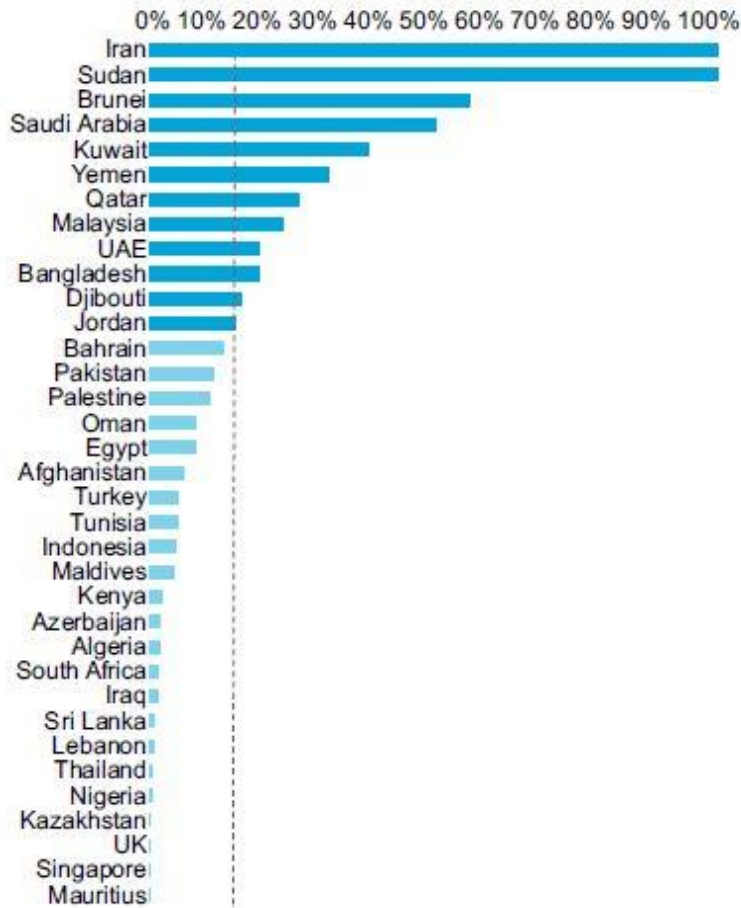
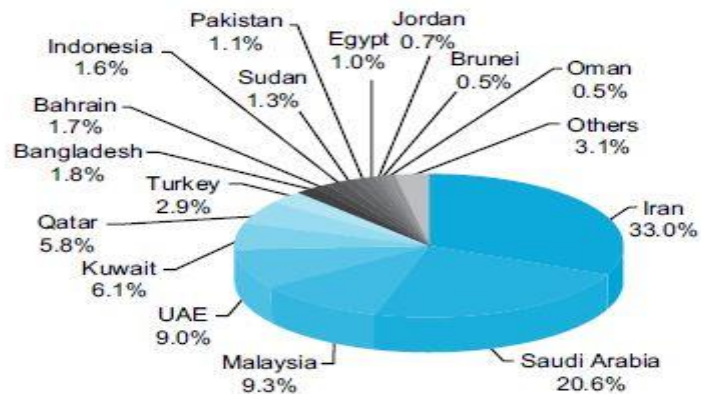


Figure 3.3.

Shares of Global Islamic Banking Assets *



* The shares are apportioned in US Dollar terms.

Source: IFSB Secretariat Workings

The value of global Islamic banking assets declined by 0.2% in 2Q2016 (y-o-y)¹². The decline is largely attributable to an adjustment to the value of Islamic banking assets in Iran, in addition to exchange rate depreciations in some key Islamic banking markets. For example, analysis of local-currency asset growth rates for Malaysia and Turkey, whose combined share in global Islamic banking assets is about 12%, shows Malaysia’s Islamic banking assets growing at 9.5% in the year to 2Q2016, and the Turkish participation banking sector’s assets expanding by 9% in the same period; the comparative growth figures in US Dollar terms for both countries are just 1.4% and 0.01%, respectively

Between 4Q2013 and 2Q2016, Islamic banking assets showed moderate growth in US Dollar terms, expanding at a CAGR(Compound Annual Growth Rate) of 9.9% across 14 jurisdictions¹³ which together represent about 94% of the global Islamic banking industry. Annual asset growth rates have rebounded in the first two quarters of 2016, growing at 9.6% and 10.9%, following a slowdown in 2015 when the Islamic banking sector grew at a modest 5.7% on average.

A similar pattern is observed in financing, with its CAGR (Compound Annual Growth Rate) recording 9.4% between 4Q2013 and 2Q2016, and showing signs of a slowdown in 2015 as it registered 6.3% expansion, but rebounding to 11.3% in 2Q2016. Deposits, while faring better than financing on both CAGR (9.7%) and 2015 rates (6.9%), had a less marked rebound in the second quarter of 2016, expanding by 8.5%, slower than assets and financing rates despite a promising first-quarter performance in which they registered a 9.4% growth rate.

Figure 3.4.

Islamic Banking Average Annual Growth Trends



The rapid growth and growth rate of interest-free banks led them to face various problems. The basics of these problems are as follows:

Legal arrangements

In the country where interest-free banks are established, interest-based financial and trade-related legal arrangements are among the most common problems. An entity operating under Islamic principles has difficulty in legally clearing interest rates, and interest-free banks are not allowed to deal with major transactions (muşaraka, mudaraba, etc.). In other words, the agreement made in accordance with the law is Islam, and the treaty, which is in accordance with Islamic law, is contrary to the legal system.

Specialist minority

Those who work in interest-free banks need to have the knowledge and skills different from those working in traditional banks and may need to be linked to Islamic principles. This is due to the fact that Islamic banks are alternatives and different from traditional banking.

While interest-free banks try to provide the human resources gap from interest-free banks, the fact that experienced employees prefer interest-free banks is contrary to their long-term career plans.

The system is new

As mentioned above, the emergence of interest-free banks has led to the fact that a number of countries and investors have not yet fully embraced this system. That is, the fact that interest-free banks do not promise any interest income at the end of the term and lack of confidence in the system creates doubt in the investors associated with the activities of these organizations.

Low number of organizations supporting interest-free banks

It is important to have supportive and related bodies in order for each banking system to be established and succeeded. There is a need for institutions and organizations consisting of economists, Islamic legal experts, management experts and financial experts to be successful in the activities of Islamic banks. The gap in this area is related to the fact that Islamic banks are new. For example, in

2001, 15 years after the establishment of interest-free banks in Turkey, the Private Financial Institutions Association was established in 2001.

Problem of income loss

Non-interest-bearing banks, in contrast to traditional financial institutions, try to cover losses with other ways, except that they do not apply extra interest rates to customers who do not pay their debts on time. For this purpose, the loan is repaid before the amount and time delay, repayment of the loan due to late payment, or repayment of the debt to the currency. Both sides should be compensated for the loss caused by delay of payment without any economic downturn.

On the other hand, although Islamic banks are deprived of additional interest income on loan repayment, in reality this problem is related to the fundamental principles of Islamic banks and serves to create convenience for customers.

Faith is prohibited in the religion and is not prohibited by law. That is why they have different meanings on the percentage. Even though Islamic religion has been allowed to compensate for it, it is not allowed to pay it.

According to Islamic jurists, additional interest rates should not be considered as interest. Because the receivable party may be compensated for the damages suffered by the debtor. But if this right is not met, the aid to a debtor who is in a difficult position is considered a deception in the religion.

Islamic banks use different ways to provide customers with flexibility in repaying loans. The most widely spread method in Turkish banks is the repayment of the loan borrower's currency. Traditional banks, which are able to delay the customer's debt, seek to earn more at a higher rate of interest. Although Islamic banks are deprived of this income, they gain the advantage of gaining an image in the eyes of their customers.

Lack of market and accounting standards among Islamic banks

Islamic banks do not have a common market. At the same time, they do not have accounting standards. The information on a bank account in a different bank

account indicates another bank's other account. Thus, it is not possible to analyze and compare the financial position of each bank.

The fact that the participation banks of Turkey are not widely spread among Islamic banks operating in different countries and the fact that interest-free banks are not properly and properly presented to the public can be considered as a negative feature of this banking system. Interest-free banks in Turkey have fewer shares in international Islamic banks. In order to increase this share, measures should be taken to increase the number of branches and ATM units of the participating banks, increase their employees' knowledge and skills. In addition, the following critical notions are offered against interest-free banks:

- Failure to make a profit share,
- The fact that the participation banks do not use the media frequently,
- Addressing a certain target audience,
- Uncertainty as a result of poor system submission,
- The similarity of procedures to traditional banks,
- The idea of making credit card applications wrong.

Problems of development of interest-free banks may also arise from their financial structure. That is, the lack of interest-free banks can become their problem. This can be summarized as follows:

Shortage of Financial Instruments: Because Islamic finance does not include interest rates, the range of financial instruments is lower than other banks. Currently, up to 1000 interest-bearing methods are used in the financial sector. An innovative Islamic finance idea should be mobilized to implement these instruments in Islamic banks.

Failure to meet urgent needs: Participating banks are not as effective as interest rate anchors in finishing the project stage and financed businesses. However, practice shows that businesses are in need of cash to meet urgent costs. The profitability and loss sharing system is not suitable for such needs. And this is one of their biggest problems.

Inability to finance long-term projects: Because long-term projects are less profitable, it is preferred to finance short-term trade through murabaha. These projects are both less risky and manageable.

It does not participate in public funding: Public funding is often implemented with interest-bearing financial instruments. For example, in Turkey there are treasury bills and government stocks. Participation banks, of course, can not do that.

Money can not enter markets: Participating banks are still unable to enter the interbank market dealing with the purchase and sale of short-term interest and liquidity financial instruments. As a result, they are deprived of the opportunity to assess their cash surpluses and to meet their daily defects.

Failure to apply credit in exchange for a document: This method, widely used in the Turkish banking system, is based on the use of interest rates and does not apply to participating banks.

Difficulties in Balance Analysis: Interest-bearing banks are not problem solving assets and liabilities with rediscount operations. The Islamic bank has difficulty evaluating the asset because of the lack of interest.

Competing with interest-bearing banks: Interest-free banks can sometimes offer interest-free banking services to their clients by creating a branch. Some international banks provide interest-free murals to Turkish companies. This turns such banks into a powerful opponent of newly emerging interest-free banks.

CHAPTER 2. COMPETITIVENESS OF AZERBAIJANI BANKING SECTOR.

2.1. Analysis of the current state of the Azerbaijani banking sector.

With the adoption of the Laws of the Republic of Azerbaijan "On Central Banks of the Republic of Azerbaijan" and "On Banks and Banking Activity in the Republic of Azerbaijan" in 1992, the legal and regulatory basis of the banking system was laid. Commercial banks are the second in the two-digit banking system, as well as in most countries in the market economy. The Central Bank stands at the first stage. The Azerbaijani banking system consists of the Central Bank and banks and other lending institutions. Commercial banks with credit institutions have the exclusive right to carry out all banking transactions in accordance with the legislation. The banking reforms implemented in the 1990s included the step-by-step implementation of prudential supervision and the improvement of legislation on transition to international standards. Special attention was paid to issues such as capital, liquidity, profitability, security of deals, use of modern technologies and management information systems.

Recently, the economic and political processes in the world require the provision of flexibility and transparency of the securities market, investment fund, banking and insurance activities, as well as payment systems, as well as improvement of regulation and supervision in these areas, as well as creation of public control system. In order to ensure that the financial system of the country is even more stable and durable, the competitiveness of the country is required to effectively ensure the financial markets, as well as protect the rights of creditors, investors and insured persons.

In order to ensure the sustainability of the financial sector of the Republic of Azerbaijan and to improve control mechanisms in this field, in 2016, the licensing, regulation and supervision of activities of the securities market, investment funds, insurance, lending institutions (banking, non-bank credit organizations and postal service providers) Financial Market Supervisory Authority of the Republic of Azerbaijan was established to improve the

supervision system in the area of control over the legalization, control of money laundering or other property, the control of terrorism financing, as well as the transparency and flexibility of the control system in these areas. The Financial Market Supervisory Authority is the first-ever legal entity to provide effective functioning of the financial markets, as well as to protect the rights of creditors, investors and insured persons. Our country, which is an integral part of the global economy, reacted quickly to the processes taking place in the global economic arena, in the face of the Azerbaijani economy, such as ensuring the financial sector's stability and strengthening control measures in this area. Ensuring the flexibility and transparency of the country's securities market, investment fund, banking and insurance activities as well as payment systems, as well as improvement of regulatory and supervisory systems in these areas is an integral part of these tasks.

At present, the Financial Market Supervisory Authority is fully functioning. Many functions of the Central Bank were transferred to the Financial Market Supervisory Authority. This process is in progress. In recent years, banks face major challenges. The devaluation of the manat, the lower the banks' performance, the decline in the revenues - all this has a serious impact on the banking sector. The government takes certain measures to soften this effect. One of them is a control system for banks through the Financial Market Supervisory Authority.

In recent years, strategic targets set by country officials include bringing banking legislation into line with international best practices and standards, ensuring the safety and health of the banking system, expanding the use of banking services, increasing transparency in the banking system, improving market discipline, and improving the effectiveness of banking supervision.

In modern conditions, the organization of the Savings Insurance Fund plays an important role in increasing the population's confidence in the banking system. The Fund's activity is considered to be an effective mechanism for the liquidation of the banking system's liquidity problem. Secondly, the fund guarantees the depositor's withdrawal from the bank's bankruptcy conditions.

Thirdly, the mass withdrawal of funds from bank accounts is avoided when the bank is bankrupt. Fourthly, deposit insurance increases the attractiveness of deposits, compared to other financial investments.

However, it should be noted that the banking system of the country, which has become a difficult situation after the devaluation of the manat in recent years, has not yet reached its destination. If we look at Standard & Poor's (S & P), Moody's and Fitch, the rating agencies in the world, the ratings of Azerbaijani banks have been downgraded. At present, some banks have denied rating agencies, and a number of banks do not generally cooperate with rating agencies.

Along with all, banks continue losing customers. Thus, the monthly report of the Central Bank indicates that the customer base of the banking sector in Azerbaijan decreased by 80,134 people or by 1.4% to 5,612,810 as of July 1, 2017. 1.4% of bank clients or 78 257 individuals were legal entities, 5 534 553 persons or 98.6% were individuals. 210,533 people or 3,8% of bank clients are entrepreneurs. In June, there was a 0.4% increase in the number of legal entities and a 1.4% decrease in the number of individuals. At the same time, the number of entrepreneurs increased by 2.4%.

The significance of determining their profitability in connection with the formation and application of new types of bank products is of great importance today. Various types of banking operations can be utilized for profitability, taking into account the characteristics of each transaction.

The offer of new banking transactions and services by commercial banks in the Republic of Azerbaijan today would allow them to increase their profits. As a result, local banks will have the opportunity to increase their revenues, not just in international practice, but at the expense of operating income.

The feature of profitability in various markets of banking services is characterized as the price of banking services. The cost of banking services is defined as transaxia expenses after the consumer is provided with the services. These payments are calculated as expense to carry out transactions.

Banks, which manage the profitability of services in different markets and segments, are actively pursuing a competitive price competition with banks that attract customers' attention to these services and offer similar services. Additionally, the pricing factor of the services is the key element of the Bank's service reputation, which creates conditions for increased customer loyalty and, ultimately, increased intangible assets of the bank.

Traditionally, it was considered that customers should use the services of a large number of bank branches. Distributed branch network, operating conditions in operating rooms, working mode and so on. has long been regarded as bank attributes.

According to the Financial Market Supervisory Authority, the banking sector's indices for December 31, 2017 are as follows:

Figure 2.1.
Assets, Liabilities, Capital indicators for the end of 2017
(in million manat)

ASSETS	31.12.2017
1. Cash resources	1,153.0
2. Correspondent accounts in the Central Bank *	2,032.2
3. Nostro accounts (correspondent accounts in other banks)	2,626.0
4. Deposits in financial institutions, including banks	7,233.5
5. Securities	2,498.5
6. Loans to financial institutions, including banks	259.5
6.1 Net loans	208.6
7. Loans to customers	11,337.6
7.1 Reserve for possible losses on loans	1,476.5
7.2 Net Loans	9,861.1
8. Fixed Assets	858.5

9. Intangible assets	128.2
10. Other assets (net of purposive reserves)	1,321.4
11. Total Assets	27,921.0

LIABILITIES	31.12.2017
1. Deposits (excluding financial institutions)	16,894.9
1.1 Deposit of individuals	7,542.5
1.1.1 Term	5,187.6
1.1.2 Required	2,354.9
1.2 Deposit of legal entities **	9,352.4
1.2.1 Term	1,710.9
1.2.2 Required ***	7,641.5
2. Claims of the Central Bank against the banks	507.6
3. Loro accounts	184.1
4. Deposits of Financial Institutions	1,515.5
5. Loans of banks	223.9
6. Loans of other financial institutions	1,891.8
7. Securities issued by banks	1,855.4
8. Other passives	1,138.6
9. Total liabilities	24,211.8

CAPITAL	31.12.2017
10. Private Equity	3,471.3
11. Total reserves	237.9
12. Total capital	3,709.2
13. Total liabilities and equity	27,921.0

Note: It has been prepared on the basis of Prudential reporting methodology

** Including funds in blocked foreign currency, as collateral for loans attracted from the Central Bank*

*** Including deposits of individuals engaged in individual entrepreneurship, without deposit of central government and municipal authorities*

**** Including current accounts of non-bank financial institutions*

The current state of the banking sector in Azerbaijan can be summarized as follows:

S (Strengths):

1. Being active on social networks:
2. Each bank has its own mission, strategy, goals
3. The volume of bank assets continued to grow at \$ 12 billion as of April 1, 2010. reached AZN.
4. Providing business loans to support small, medium and large businesses in business

W (weaknesses)

1. Banks' business is not client-oriented, product and service-oriented. New products were produced, offered, but the customer was always outside. From the moment we gained independence against banks in the country, there was no trust and no longer. People prefer to keep tens of thousands of pounds under their pillows, which has a bad impact on the banking sector. After devaluation, there have been many conflicts between banks and people that can not resolve these conflicts right now. And in those conflicts, our banks hit the bottom of customer satisfaction.
2. Non-control over the spending of the loan given to the customer. As a result, the total amount of "Overdue Loans" reached 1 billion 592.9 million manat as of September 1, 2016. Compared to the beginning of 2016, overdue loans have grown

by at least 5.6 percent and an annual rate of 19.4 percent. In order to avoid this, they must be strictly controlled.

3. High credit interest rates. At present the average loan's FIFD is 25%. One of the reasons is that the deposit is at 10% per annum. If the loan interest rate is low, the number of banks will increase and will have a positive impact on the bank's revenues.

O (Opportunities)

1. State support to banks. State Oil Fund holds auctions with dollars. For example, the "20th of September 2016" auctioned out \$ 100mln worth of funds and sold \$ 72.4 million to 20 banks

2. Consecutive increase of the minimum capital requirement of the private banks by the Central Bank and promoting the consolidation process strengthened the private banking system's capital base and ensured the banking system's lengthening.

3. Decrease in the number of banks. Decrease in the number of competitors will increase the market share of other banks in the banking sector. New customers can access. State support to banks. State Oil Fund holds auctions with dollars. As an example, the "20th of September 2016" sold auction of \$ 100 million and sold \$ 72.4 million to 20 banks.

T (Threats)

1. Decrease of people's confidence in banks. On January 1, 2016, the total amount of savings in banks was 9473.9 million manat, while "September 1, 2016" was 7931.9 million manat.

2. Increase of the authorized capital of banks. With a decision of the Central Bank Board dated November 14, 2013, the total capital of the banks is \$ 50 million. delivery to the bank leads to the closure of the banks with a share capital of less than 50 million manat.

Looking back at recent years, we see that economic entities have continued to expand their access to financial services, and the level of use of financial infrastructure has risen. The number of bank service points per 100,000 people has

reached 10. Taking into consideration the branches of "Azerpocht" providing financial services to the population, this figure is 20. In 2014, 47 new branch offices were opened, of which 34 were in the regions. More than half of the bank branches are concentrated in the regions. In order to stimulate alternative sources of lending, the Central Bank has also supported non-bank credit organizations this year. The number of non-bank credit organizations reached 157 and the number of their branches reached 222. In order to improve the service provided by the Central Credit Registry (CCR), two service points of the CCR started operating at ASAN service centers.

Protection of the stability of payment systems, expansion of the scale of application of modern infrastructure in this area and the promotion of innovations have been one of the major activities of the Central Bank in 2014. The volume of payments made through the National Payment System in 2014 was 2 times the GDP. Expansion of the "Government Payment Portal" established within the framework of "e-Government" was continued. As a result, 19 organizations have been integrated into the portal. Payments are made on more than 285 types of services provided by these organizations. The number of payment cards emitted in the country is 5.9 mln. number of ATMs reached 2586, number of POS-terminals reached 68676. The number of payment cards increased by 5%, the number of ATMs - 6.8%, the number of POS-terminals - by 2 times.

However, for the full development of the banking system in line with world standards, the Central Bank and credit institutions of the country have to constantly expand their operating environment, to provide high-end automation and computerization, timely banking system, and to achieve high quality and high quality customer service.

2.2.Competitiveness of Azerbaijani banking sector.

In the market economy, the country's banking system is an integral part of the national economy. The banking system, consisting of the Central Bank and credit institutions, ensures the implementation of settlements between economic entities irrespective of their ownership relations.

It is impossible to imagine the world economy beyond the banking sector. Because the banking sector is the most promising and stimulating area in the economy. When planning international or regional projects, it is necessary first of all to calculate its economic basis: how much money will be allocated to the project, how long will this money be repatriated, what will be the material gain, and so on.

Commercial banks play a leading role in the banking system. All of these banks operate as "universal banks", providing customers with various banking services. The development and improvement of the banking system is carried out in line with the development of the Central Bank in line with world standards, as well as meeting the modern requirements of private banks.

Recent events in the banking sector of Azerbaijan have an impact on all economic sectors in the country. That is, when the banking sector is limiting lending, economic activity in the country is weakening, people have difficult access to the market, and as a result trade turnover diminishes. The episcenter of all these events is the banking sector. Therefore, the banking sector can be considered not only as the locomotive of the Azerbaijani economy, but also of the world economy as a whole.

The banking sector is an integral part of the last 15 years of the Azerbaijani economy. Comparing the activities of the banking sector in the early years of our independence with the present period, a completely different perspective on our eyes revives. As the other fields of the country's economy develop, the banking and financial sector has also developed to meet new needs. But, unfortunately, the confidence in banks in recent years, especially in the development of the Azerbaijani economy, has not fully acceded. In particular, high credit rates in

banks, unpleasant actions by some banks that use financial literacy, and illegal operations resulted in bankruptcy. Most Azerbaijani citizens were damaged by such unprofitable activities of banks. It is no coincidence that the president mentioned one of the speeches that made the banking sector the most hit economy of Azerbaijan.

Serious reforms have already begun in the banking sector, as well as in different sectors of the country's economy. Increasing the role of banks in economic development and increasing diversification of the non-oil sector, raising credit investments in the sector by accurately evaluating the demands of the real sector, particularly the non-oil sector, to ensure that business entities in all regions of Azerbaijan, as well as the population access to quality financial services, purposeful work is being carried out to expand the scale of electronic banking.

In 2015-2018, about 11 banks were closed in Azerbaijan, and their liquidity was worse than the downside, and banks had no choice but to close down. In the meantime, insured deposits have been insured for the last three years, regardless of the amount and interest rate, to avoid damaging our citizens. Because about 1 billion manats of the bulk of the population were in these banks. Just after that decision, both people and their savings were able to escape great damage.

According to Financial Market Supervisory Authority, the number of branches of 30 banks operating on January 31, 2018 was 511, the number of branches was 142, and the number of ATMs was 2,439. In total, the banking sector staff comprised 16,207 people.

At present, 30 banks operate in Azerbaijan under the Financial Market Supervisory Authority's license:

Figure 2.2.
Operating banks for the beginning of 2018

1. "ACCESSBANK"	16. "GunayBank"
2. "AFB BANK"	17. "XALQ" Bankə
3. "AGBank"	18. "Kapital Bank"
4. "Amrahbank"	19. Bank Melli Iran Baku branch

5. "AtaBank"	20. "Mupanbank"
6. "International Bank of Azerbaijan"	21. "Naxçəvanbank"
7. "Azerbaijan Industry Bank"	22. "NBCBank"
8. "Azer-Turk Bank"	23. "NƏKOYL"
9. "Bank Avrasiya"	24. National Bank of Pakistan NBP Baku branch
10. "Bank of Baku"	25. "Paça Bank"
11. Bank "BTB"	26. "Rabitəbank"
12. "Bank Respublika"	27. "TURANBANK"
13. Silk Way Bank	28. "UNƏBANK"
14. BANK VTB	29. "Yapə Kredi Bank Azerbaijan"
15. "Expressbank"	30. "Ziraat Bank Azerbaijan"

Azerbaijan Banks Association reports that assets, loan portfolio and profit-earnings report for the current period of 2016-2018 in Azerbaijan are as follows:

Figure.2.3.
Assets for the current period of 2016-2018

Banks	Assets (mlnAZN) for	Assets (mlnAZN) for	Assets (mlnAZN)
International Bank of	8695.1	12223.7	13241.7
PAŞA Bank	3551.8	3138.8	2122.9
Kapital Bank	3184.5	3096.7	2017.4
Xalq Bank	1813.6	1668.6	1598.0
Azerbaijan Industry Bank	945.2	787.2	685.3
AccessBank	844.8	1058.9	1188.8
Rabitəbank	727.2	552.3	450.7
Bank Respublika	702.1	912.1	893.6
AtaBank	625.9	472.5	598.3
Unibank	601.8	716.6	835.3
AFB Bank	494.6	300.4	312.6

AGBank	488.4	520.0	540.3
Muğanbank	480.2	470.8	564.3
TuranBank	477.3	528.2	523.1
Nikoil Bank	437.3	439.7	589.5
Yapı Kredi Bank Azerbaijan	427.3	443.1	469.3
Silk Way Bank	411.3	404.0	362.0
Bank of Baku	399.9	549.6	734.8
Bank VTB	397.2	435.6	469.9
Azer Turk Bank	335.2	469.5	671.9
Expressbank	314.3	286.9	318.5
Bank BTB	268.8	241.5	211.0
Amrahbank	204.8	256.2	304.1
NBCBank	204.1	159.0	167.3
Günay Bank	192.2	285.9	94.3
Ziraat Bank Azerbaijan	186.7	132.2	90.2
Bank Avrasiya	151.2	143.4	123.3
Naxçıvanbank	141.9	126.4	95.1
Bank Melli Iran Baku branch	100.5	80.5	101.3
National Bank of Pakistan NBP Baku branch	11.7	11.3	11.0

Figure2.4.
Credit Portfolio for the current period of 2016-2018

Banks	Loan Portfolio for the Beginning of	Loan Portfolio for the Beginning of	Loan Portfolio for the Beginning
International Bank of	1784.4	5503.9	6872.9
Xalq Bank	1312.2	1274.5	1330.7
Kapital Bank	1244.0	1267.0	1104.0
PAŞA Bank	943.1	870.2	690.2
AccessBank	503.5	598.8	922.8
AtaBank	464.0	406.5	525.0
Silk Way Bank	375.6	388.3	335.7

Muganbank	349.1	346.0	380.4
Azerbaijan Industry Bank	298.8	297.4	152.3
Nikoil Bank İKB	291.0	340.3	370.2
AGBank ASC	282.9	292.2	410.2
Bank VTB	281.2	321.1	419.6
Unibank	280.1	426.6	597.5
TuranBank	266.8	282.5	290.6
Rabitabank	234.6	205.2	306.4
Bank Respublika	229.6	283.2	323.8
AFB Bank	218.1	225.4	169.2
Bank of Baku	197.7	252.3	575.9
Expressbank	167.6	199.3	275.2
NBCBank	154.4	121.0	153.0
Yapı Kredi Bank Azerbaijan	146.0	212.3	263.4
Gunay Bank	139.5	217.2	93.7
Bank BTB	130.9	144.0	89.9
Azer Turk Bank	119.7	149.3	418.3
Amrahbank	95.2	164.6	153.6
Bank Avrasiya	85.3	90.2	81.8
Ziraat Bank Azerbaijan	67.9	54.7	11.2
Naxçıvanbank	63.4	61.6	52.9
Bank Melli Iran Baku branch	3.4	7.2	17.2
National Bank of Pakistan	1.6	1.8	2.2

Figure2.5.
Net Profit (Loss)for the current period of 2016-2018

Banks	Net Profit for the Beginning of 2018 (AZN	Net Profit for the Beginning of 2017 (AZN	Net Profit for the Beginning of 2016(AZN
International Bank of	806.0	-1356.5	-20.1
Kapital Bank	94.8	52.4	63.9
PAŞA Bank	59.0	61.0	3.0

Xalq Bank	17.6	10.4	2.2
Yapı Kredi Bank Azerbaijan	10.1	-10.3	-4.5
Bank Melli Iran Baku branch	6.9	-29.3	0.5
Bank Avrasiya	6.4	0.9	0.5
Bank VTB	4.8	-2.6	-36.5
Azerbaijan Industry Bank	4.4	4.8	2.6
Gunay Bank	4.1	-4.7	-3.6
Ziraat Bank Azerbaijan	4.1	6.0	3.5
Unibank KB	4.0	-31.3	1.5
Naxçıvanbank	3.6	8.4	8.4
Silk Way Bank	3.0	1.6	1.5
NBCBank	2.9	-1.8	-13.8
Expressbank	2.0	0.4	0.7
Azər Türk Bank	1.1	7.3	-4.6
Bank BTB	0.7	-13.1	-1.6
AtaBank	0.4	0.3	1.0
National Bank of Pakistan NBP Baku branch	-0.1	0.0	0.0
TuranBank	-0.7	-1.4	0.1
Nikoil Bank İKB	-2.7	-148.5	-9.1
Muğanbank	-6.3	-14.0	0.4
AGBank	-6.7	-35.6	-38.2
Amrahbank	-8.6	-8.4	-6.2
Bank Respublika	-10.5	-34.6	-7.7
Rabitəbank	-11.6	-12.9	0.0
AFB Bank	-12.2	2.6	2.1
Bank of Baku	-35.4	-15.3	-23.0
AccessBank	-56.4	-110.7	1.7

The presented material once again shows that in the country's banking sector, there are also many suspicious factors that have a negative impact on their banking activity, which is likely to make it worse in the future. This is primarily due to the ongoing currency and credit risks, weak management services,

protecting creditors' rights, increasing the bank's confidence in the population, and so on. is showing itself.

Shortage of long-term resources, weak investment attractiveness of the banking sector, weak links with its production areas, weak securities market presence and other issues are one of the serious problems of the banking sector in the country. The current state of the country's banking sector is closely monitored by international financial and credit experts. For example, the experts of the European Bank for Reconstruction and Development (EBRD), in their reports, positively assessed the liberalization of "capital flows" in the Azerbaijani banking system, as well as strengthening the control over the banking sector. According to the assessment of the international rating agency Fitsh IBCA, Azerbaijan's high risk category has been assigned to MPI3. According to the analysts, the Azerbaijani banking system should pay more attention to the proper determination of the exchange rate of "AZN in national currency". The course of today's manat is very scary due to the high price of oil in the world market, which can be dispersed at any time as it collapsed in 2015.

Meanwhile, Fitsh IBCA, a well-known rating agency, pointed out that while comparing commercial banks, the International Bank of Azerbaijan has higher results both in the republic and in the South Caucasus region.

The weakness of the banking sector in Azerbaijan is the low efficiency, the existence of problematic loans, the existence of non-cash settlements in banks, the lack of credit resources in the non-oil sector, the high credit risk in general. in particular. The weak participation of the country's banking sector in the real economic sector, the low share of bank assets in GDP, and the lack of credit investments for the development of financial spheres are more evident both in the CIS and in the Baltic countries. That is why in 2015, the devaluation of the national currency "manat" in Azerbaijan took place, its purchasing capacity decreased to 2 times. This once again shows that the non-oil sector in economic development is still weak, and we depend more on the oil and gas factor. Therefore, the fall in oil prices by more than 3 times in the world market made it

necessary for the budget to be revised. The banking sector of our country should take an active part in anti-monopoly activities, taking into account the development of socio-economic development within the framework of the global economic crisis. The level of capitalization of commercial banks does not allow them to lend credit to the real economy. In the near future, the banking sector of the country should be ready to address the existing problems at the same time, adequately respond to new requirements in a globalizing world.

Since economic globalization is a modern requirement, it encompasses all aspects of the global economic system and the deepening of international economic relations has made it important for the financial system to join these processes. The impact of this phenomenon on the financial market is linked to the integration of national financial markets into the global financial markets. Globalization of the international financial system is explained by the processes taking place in the world economy in recent decades. The development of regions and nations in the near future depends largely on the integration of mutual economic and financial relations.

As a visual example of financial globalization, it is possible to demonstrate the limitations of capital over national accounts over current transactions. This process has also been joined by Eastern European countries, the Commonwealth of Independent States and the Republic of China since the 1990s. The role of financial globalization in the global economy can be seen in the global financial market at the beginning of the 21st century when it comprised 37.6 trillion dollars (83.6%) of the Gross Domestic Product. It should be borne in mind that the global economic globalization has led to the introduction of standards in the banking activity, the freedom of movement in the movement of capital, the elimination of various restrictions, the widespread use of computer technology and other positive changes.

In the early 1990s, Azerbaijan's economy was trying to attract more foreign investment, and in modern times we are involved in financing various projects in Georgia, Turkey, Russia, Kazakhstan, Ukraine and other nearby countries.

It is known that at the moment small and medium-sized businesses face some difficulties due to high interest rates offered by banks. Interest rates are so high that it reduces the profitability of a project that the entrepreneur wants to implement, and sometimes causes them to become bankrupt.

In Islamic banking, the borrower is paid at no interest, and the bank pays the share of the bank in return for the amount of money he / she receives when he receives only income. The bank also participates in the elimination of the loss if the borrower suffers losses for a variety of reasons. In modern times, Islamic banks are on the verge of progress.

These financial institutions, guided by Sharia law, propose to develop business ethics in the form of partnerships. Here it is forbidden to collect deposits and make interest-lending process by depositing. Currently, more than 300 Islamic banks are operating in more than 50 countries around the world with assets up to one trillion dollars. The methods of income generated by Islamic banking are based on partnership, mutual benefit, repayment of losses through repayment, repayment of borrowed funds, lease of acquired property on preferential terms, prevailing leasing transactions, determination of ownership relationships through Islamic securities, services such as opening.

It is important to use the experience of Islamic banking in the development of Azerbaijan's banking system. In general, Azerbaijan has bilateral foreign economic relations with more than 90 countries. A special place in foreign political and economic relations is divided between the Islamic world. Despite the fact that religion is separated from the state in Azerbaijan, the vast majority of the population are also interested in Islamic banking, following the Shari'ah rules and Islamic banking.

2.3. Banking sector development problems.

The banking system of the Republic of Azerbaijan consists of the Central Bank of the Republic of Azerbaijan, credit institutions and Financial Market Supervisory Authority which was established in 2016. The Central Bank is the central bank of the state and its activity is governed by the Constitution of the Republic of Azerbaijan, the Law of the Republic of Azerbaijan "On the Central Bank of the Republic of Azerbaijan", the Civil Code of the Republic of Azerbaijan, this Law and other normative legal acts adopted in accordance with them, as well as international agreements to which the Republic of Azerbaijan is a party . Activities of credit organizations in the Republic of Azerbaijan are regulated by the Constitution of the Republic of Azerbaijan, the present Law, the Civil Code of the Republic of Azerbaijan, the Law of the Republic of Azerbaijan "On Nonbanking Credit Organizations" and the Law of the Republic of Azerbaijan "On Credit Unions", other normative legal acts of the Republic of Azerbaijan, Regulatory acts of the Bank, as well as international agreements to which the Republic of Azerbaijan is a party.

Uncertainties over the past few years have resulted in the elimination of legal and administrative barriers in the early years of independence in Azerbaijan and the banking sector has been developing rapidly in supervision, supervision and coordination of the Bank. In the past year, the services provided by the banking sector have been rising, increasing in quality and efficiency. However, it is crucial to further improve the legal and administrative arrangements that have been implemented, to improve the types and quality of services provided, and to use the experience of the vibrant country in this area.

Major Problems in the Banking Sector The financial department in Azerbaijan is vulnerable to structural vulnerability. It is seen that the population is more attractive in trade. But there is not enough financial resources for this. After the crisis in the country (in 1992-1993 and in 2015-2016), people's confidence in the banks has dropped significantly. In this case, those who have good financial

position will be able to direct this opportunity to non-bank financial instruments. Some people spend their money on lending to banks. The problem of liquidity (cash) is at the top of the problem of the banking sector. These banks, which do not have the required commercial banks, the branch offices and the broad division, have the same capabilities as well.

Azerbaijan is continuing its rehabilitation activities with state banks trying to create its own banking system. The combination of three of the four main banks of the Soviet era was only possible in 2000. In particular, it has been included in the privatization scheme in banks that have a great deal of importance in the economy. However, the full integration of the International Bank has not been held in 2013. Reforms in the Banking Sector Reforms in state banks; World Bank's SAC program is being implemented with the aim of developing management, development of new services and markets, and the development of banks. On February 16, 2001, the Bank established the AZIPS system for banks to use more rapidly within the country and implement on-line system. This system is based on SWIFT in accordance with international standards.

In order to eliminate shortcomings in the banking sector, the government has prepared a program in 1999 with the participation of the World Bank and the International Monetary Fund. The main objective of this strategy is to provide an infrastructure of a well-developed and up-to-date infrastructure that is well-balanced and competitive, including re-structuring and privatization of state-owned banks, consolidation of private banks, increasing regulatory and regulatory frameworks of the Bank, and accounting. Bank reforms have been implemented to increase financial assistance to small and medium-sized businesses in the country. With a view to raising the bargaining, the process of directing foreign investment to the banking sector has been significantly reduced.

Starting from January 2005, banking system "Internet Banking" and "Mobile Banking" has been introduced in Azerbaijan. These activities were largely based on the recommendations of the World Bank and the International Monetary Fund. At present the international banking services are being developed in the

Azerbaijani banking market while the capabilities of its clients are developing. In order for the banking sector to develop in the country and to regain public trust in the banks, an insurance fund must be established and a bill on insurance of banks must be adopted. Some reforms are underway to insure that insured mortars are safeguarded.

The Law on the Establishment and Operation of the Fund of Insurance of Insurance was issued in 2005. For problems arising from the activities of a fund other than the Bonds Insurance Fund, the Bank should pursue a policy of disclosing adequate disclosure to the Bank's other financial resources. The banking sector continues to work on infrastructure work, payment system, accounting system, banking supervision and legal infrastructure. The development of the banking sector will allow the Bank to benefit from the Bank's services in terms of its separate segment, particularly in terms of easy loan accessibility. The development of the banking sector and the reputation of the system will have a negative impact on the ability of banks to cash in on their funds.

Presently, banks provide a wide range of services to their clients and retail banking services are rapidly developing. Bank products are offered by the most up-to-date technological means such as internet-banking, sms-banking, mobile banking, automated bank kiosks.

The banking system's regional network and access to financial services are rapidly expanding, and banks have been active in international financial markets. The prestigious financial institutions of the world, which have been operating since 2007, are allowed to operate within the country by representative offices of Commerzbank and Citi Bank and advanced banks of other developed countries (such as AccessBank, Bank VTB Azerbaijan, Ziraat Bank Azerbaijan, etc.) , which has contributed to the application of the world's most advanced banking technologies in Azerbaijan.

During the transition to the market economy, there has been a radical change in the source, structure, and use mechanism of all types of banking resources.

Major changes in the modern banking system can be grouped as follows:

- Reforms in the banking system have further increased the rights and responsibilities of state and commercial banks and enhanced their regulatory mechanisms;
- The role of banks and management functions in regulating money circulation have increased;
- Establishment of joint banks with the ability to compete with foreign banks in the country;
- The Central Bank has the right to issue a free monetary policy and issue money to circulation.
- Banks deal with new types of activities, conduct transactions with securities, leasing, factoring and so on. expanded access to operations.

As a result of the loans provided by the banks in the modern market economy, financing of various sectors of the economy is one of the key elements of the role of the banking sector in the development of the economy (eg, construction of new buildings, schools, roads with banks' which affects the increase in production, the employment of the population, and consequently, the inclusion of taxes to the state budget).

In addition to loans, banks are considered to be one of the main instruments in the monetary policy pursued by the Central Bank. Thus, through the banks, the Central Bank implements money emissions, regulates the circulation of money in circulation. The deposit of money from the population by the banks prevents additional cash outflows, that is, the connection between those who have some kind of money and those in need of money.

Providing cashless settlement by banks allows for easy execution of settlements both inside and outside the country.

Thus, the successful implementation of the tasks kept the positive dynamics of the development of the banking system and strengthened the role of banks in the financial intermediation.

It should be noted that there are some shortcomings and deficiencies in the banking system and their elimination can lead to the further increase of the role of the banking system in the economic development of the country.

It would be expedient for the following measures to be taken to address these shortcomings and shortcomings:

- Improvement of the Bank's legislation and its incorporation into a single system;
- Reduction of loan interest rates in banks and non-bank credit institutions;
- The banks are not more lending-oriented;
- Increasing the range of bank products.
- Reduction of insurance premiums on debit (credit) cards issued by banks;
- Revitalization of the securities market (stock market);
- Taking relevant steps in the preparation of the professional staff.

The dynamic development of our country involves systematic and rapid reforms in the banking sector, including the introduction of new banking technologies, the provision of new services, the greater involvement of economic entities in the banking and financial circulation. For successful implementation of these tasks, there is a need for a joint solution to common problems for commercial banks, further deepening of their cooperation with state and non-governmental organizations, and more active business relationships with international financial institutions. The Central Bank has gained considerable success in forming the country's banking system, its market management tools, and administrative methods. Nevertheless, the new era puts new tasks. Today, the application of self-development mechanisms in the banking sector is more relevant than previous periods. The mission of the Association (its main objective) is to provide the effective representation and protection of the common interests of banks and non-bank credit institutions in the state and non-governmental organizations and to the dynamic development of member-organizations on the principle of self-governance. To achieve these goals, the main task of the Azerbaijan Banks Association is to create and improve self-development mechanisms. In this regard,

it is an objective necessity to accelerate the institutional development of the ABA and to strengthen its role in the country's economic reforms.

CHAPTER 3. ECONOMIC PROSPECTS OF APPLICATION OF ISLAMIC BANKING IN AZERBAIJAN.

3.1. Economic Perspectives of Islamic Banking Application in Azerbaijan.

After the independence of the Republic of Azerbaijan, many sectors of the economy have begun to develop rapidly. The development of the banking system should be emphasized in the meantime. In particular, we should note that the banking system is developing faster and more competitive in other areas of the economy. One of the new areas of activity is the development of Islamic Banking in Azerbaijan.

Cooperation with the Islamic Development Bank (IDB) in the use of funds of interest-free banking institutions is particularly important in the development of the Azerbaijani economy. Thus, membership of Azerbaijan on 04.07.1992 promoted the acceleration of mutual cooperation.

At present 9,76 mln. The US dollar (0.13% of the total equity capital) is closely involved in its business. Relations between Azerbaijan and other Muslim countries with the Islamic world were not firm during the Soviet Union. The reason for this was the unyielding attitude of the Union to the religion and the materialist management style. As regards Islamic banking and finance, this area was not so popular and remarkable in those years. This type of financing emerged from the end of the 60s of the last century and has been on the development stage for a long time.

After re-establishing its independence in 1991, Azerbaijan has been a member of many international organizations. One of them is the Islamic Development Bank, which has a leading role in Islamic banking and finance. With regard to relations with countries with the majority of Muslim countries, rich oil exports, this has widened even after the signing of the Treaty of the Century, particularly in 1994. This contract brought Azerbaijan to the financial world and later created an influx of investors from the Persian Gulf countries to our country. Over time, along with traditional banking systems, Islamic Development Bank,

Kuwait Arab Economic Development Fund, Abu Dhabi Development Fund, OPEC Fund for International Development, Saudi Fund for Development and others. financial institutions expanded their activities in Azerbaijan. They mainly focus on improving the living standards of refugees and internally displaced persons, construction of schools, laying water channels, supplying areas with water, repairing roads, reconstruction of power plants and so on. implemented projects in the field. While implementing these projects, they are leasing, term sales, preferential credit lines and so on. such as Islamic financing services.

Today, there is a great potential for the successful development of Islamic banking in Azerbaijan. Therefore, many Azerbaijani specialists do their utmost to implement Islamic Banking in our country within the framework of existing legal and regulatory framework. With the help of the Islamic Educational and Research Institute, which is a member of the Islamic Development Bank, a number of Azerbaijani universities and organizations are organizing various events in the country or participating in seminars abroad. Also, the Bank's Technical Cooperation Office, and the Islamic Financial Services Department, also bear fruit in this business. They create conditions for staff members of relevant government agencies, staff from different public and private banks to conduct training abroad, and provide financial support to them. Nevertheless, there is still a lack of expertise in this field in the country.

Despite all the difficulties in Azerbaijan, there are some improvements in the Islamic banking sector. The Islamic Corporation for the Development of the Private Sector, which is a member of the Islamic Development Bank and is a member of Azerbaijan since 1999, has extensive activities in the country. This organization is closely cooperating with local banks in our country. Since 2006, the corporation has been providing leasing (leasing), leasing, leasing and subsequent sales for small and medium-sized businesses, such as International Bank of Azerbaijan, Unibank, Bank Standard, Rabitabank, Turanbank, Azerdemiryolbank with 17 mln. US dollars. During the credit lines, both parties agreed that a single penny would not be directed to the areas where the Sharia was forbidden. These

transactions are not contrary to the Azerbaijani legislation and remain "confidential" under the conditions of the traditional banking system. Interest in this type of credit line is growing.

Another way to explore the Islamic finance potential in the country was the creation of an investment company operating on these bases in Azerbaijan. This was evident in the company founded by the Caspian International Investment Company based on the principles of Sharia, which was founded in 2008 with the fully owned state-owned Azerbaijan Investment Company and the Islamic Corporation for the Development of the Private Sector, the Islamic Development Bank. In the newly created company, the Corporation's shares are 75% and the Azerbaijani Investment Company is 25%. Since the new company is a non-bank institution for its technical structure, it will be easier to implement investment projects and projects that meet Sharia laws. The main objective of the company is to strengthen its export potential by involving foreign and local investment in the non-oil sector of Azerbaijan. It is believed that the share capital of the company will be increased from the current 4 million to 70 million in the near future. The company will be supported by both the government and international financial institutions through the potential of both leading shareholders.

In general, the Islamic Development Bank Group is closely involved with the region. That is why the Bank decided to hold its 35th Annual Meeting in Baku in summer 2010. In addition to the Islamic Development Bank Group and Arab funds, a number of other Islamic financial institutions are also investing in the development of the Azerbaijani economy. they are interested.

In general, the Islamic Development Bank has provided preferential loans to Azerbaijan for over \$ 130 million in various years, providing humanitarian assistance to refugees and internally displaced persons, building schools, manufacturing facilities, water channels and roads, and feasibility studies for socio-economic development projects the total amount of \$ 5 million was disbursed without funding.

Up to now, IDB has invested about \$ 1 billion in 18 projects within the Azerbaijani economy. Agriculture, energy, transport, social, water supply and so on. 14 of these projects have already been completed and 4 projects are in progress.

Some aspects of the economic cooperation between the Islamic Revolution Bank and Azerbaijan can be summarized as follows:

At the expense of loans allocated by the Bank

a) implemented projects:

1. Construction of Mingachevir hydroelectric power station
2. Construction of Mil-Mugan Collector
3. Construction of the Xanarx Canal (1st stage)
4. Construction of Alat-Gazi-Mamed highway
5. Rural Areas Development Project

b) Projects being implemented:

1. Construction of the Xanarx Canal (Phase II)
2. Reconstruction of Ujar-Yevlakh highway
3. Rehabilitation of infrastructure facilities suffered as a result of the earthquake
4. Construction of "Khachmaz" s / s from 330/110/10 kV and connection of 330/110 kV to Yashma-Derbent power transmission line
5. Construction of the Valvala River-Takhtakorpu section of the Samur-Absheron canal
6. Construction of Yevlakh-Ganja road

At the expense of grants allocated by the Bank:

a) implemented projects:

1. Preparation of a working project for the construction of the Alat-Gaza Mammad road
2. Preparation of Samur-Absheron irrigation system reconstruction scheme
3. Reconstruction project of Lankaran canning plant. Preparation of technical feasibility study
4. Reconstruction of Khirdalan Dairy Plant

5. Preparation of Bid Document and Consultant Services in Connection with the Implementation of the Contract for the Purchase of Equipment to be Used in the Mingachevir Energy Project

b) Projects being implemented:

1. Strengthening the Capacity of the Ministry of Finance
2. Strengthening the Capacity of the Ministry of Economic Development

3.2. Experience of foreign countries in the application of Islamic banking.

The term "interest-free banking" covers a wider area than the concept of Islamic Banking. Because there are Islamic banks in several countries of the world that have been set up for various purposes but can not be described as Islamic. The intensive practice of Islamic financial law among Arab countries is being implemented in a number of Arab countries today (Saudi Arabia, UAE, Kuwait, etc.). But in 80-90s of the twentieth century, the process of applying the Islamic finance law in accordance with the purposeful Islamization of Islamic banking and the Sharia traditions was first of all developed in Iran.

The Islamic banking activity in Iran came into force on March 21, 1984. In 1984, the Islamic Finance Council (Islamic Consultative Assembly) adopted the Islamic financial right to be used in practice. According to the adopted legislative acts, until the end of March 1985, the entire financial institutions Islamization was carried out. However, the full implementation of the new principles and requirements for banking regulation and control in practice actually required more than five years and was completed only in the early 90s of the last century. The practice of adding and holding the deposit and interest rates has been squeezed out of the operational and investment activities of the bank removed. Today, country banks offer Islamic deposits (current accounts), Islamic savings accounts (savings deposits) or Islamic long-term investment deposits until demand deposits are requested. Until required, deposit and current account holders will be able to use a checkbook (opened account amount) and checks with checks. Owners of collection accounts and savings deposits also use certain preferences in terms of their ability to obtain financial resources and loans. The incentives and privileges of deposit holders and depositors are also covered by the Islamic banks financing the account holders of Mecca.

Today, a full reform of the national credit-banking sector is underway in Pakistan, which is closest to the practice of Iran. Here is a very strict Islamization model, similar to the Iranian model, in the extremely short period of time, the same

means and methods are used for substantial reorganization of the whole credit-banking system.

Since 1983, the legal framework for the establishment of Islamic Banks has been formed in Malaysia as a result of improvements in national legislation. There are also many Islamic banks in this country.

With the adoption of the Law on "Private Financial Institutions" in the Republic of Turkey in 1984, the country also has a great opportunity to operate on Islamic banking principles. Following this incident, private financial institutions such as Faisal Finance and Al-Baraka Turk started functioning since 1985.

The processes of the lending-banking sector are being developed in different Arab countries in different intensities. Among them, the mechanisms of banking business were practiced intensively in Pakistan after Iran over the past decade. In December 1999, in Pakistan, the Supreme Court considered that any additional calculation and holding of interest on the debt would be contrary to Islamic moral norms, and the government set up a fully-fledged financial and credit-banking system incorporated in the country until mid-2001. The transition of the country's banking practice to new principles in the shortest possible time has led to the deterioration of the banks' deposit and investment activity, especially in the initial period. Also, the individual entrepreneurship sector, particularly small firms, individual entrepreneurs and single owners, closely cooperated with banks because the actual value of the financial resources attracted from them began to increase substantially. At the same time, the cancellation of interest in the formal banking sector often resulted in an increase in the loan value in the informal (usury) debt market and the banking sector. Even with the necessity of obtaining borrowing resources from local small private individual entrepreneurs, parallel activities of the "black financial market" have begun to expand. Large industry owners and businessmen have been worried that the position of the public sector in the local credit market is likely to be substantially strengthened within the framework of the country's banking reforms based on full funding of financial and credit-banking structures. On the other hand, large private entrepreneurs and

investors often avoid the use of Islamic financing methods requiring them to fully disclose their real balance sheet, first of all, about the actual amount of profits they receive as a result of their investment project. The ability of the Islamic Bank to obtain real-world information about the entity's actual borrowing, as well as many other information about the entity's business, is usually less restrictive, weakly aligned, and often less profitable for Islamic banks to make the most appropriate investment decision. Local individual entrepreneurs and investor management capabilities are very weak, they are characterized by a lack of formal behavioral ethics, timely commitment to commitments, which makes the PLS principle objectively difficult to implement in Islamic banking operations. The situation was complicated by the fact that, first of all, banks and financial institutions that underwent new Islamic financing principles were automatically transferred under state control or directly to the public sector. However, the Pakistani government, acting in line with the general strategy for strengthening national individual entrepreneurship, is no longer exaggerating the likelihood that a number of Islamic banks and other Islamic finance and credit agencies will be privatized. The most serious problem of banking reform on the basis of full crediting of the national credit and banking sector is that the real intervention of the state ("nationalized") banks in the management, operation and investment of local private debt lenders can strengthen the already severe corruption problem in Pakistan. The real prospects of full-fledged finance and credit-banking structure are largely dependent on whether the government's economic and investment activities in the country, at the same time, undermine the credibility of private investors against Islamic banks.

In all Islamic countries, except for Iran, Pakistan and Sudan, national banks are guiding traditional banking principles in their operations. For example, in Bahrain, Malaysia, which is considered to be the second financial center of the Muslim world, Islamic banks are parallel with traditional banks.

At the end of December 2000, bankers' consultations were held in Labuan Island, Malaysia, Saudi Arabia, Kuwait, Malaysia and other Muslim countries, and

decided to establish an Islamic financial market. Its shopping areas are located in Bahrain and Labuan.

Thus, we have noted that the Islamic financial institutions have an increasingly important role in the global financial system. At the same time, traditional Islamic finance products are relatively easy by ordinary banks. Also, the banking system is a trademark of banking and banking services.

Islamic financial institutions are widespread in the world as demand grows, as well as accumulation of sufficient financial resources by several Muslim countries. It is likely that there will be trends in the development of Islamic banks, as exporters continue to receive substantial revenues, financial markets of Islamic countries are developing, and western companies compete in attracting foreign investors. All of this creates the basis for deep study of Islamic banks' performance and their introduction to traditional financial markets.

Thus, the aggregate assets of banking institutions operating on the principles of Islamic banking worldwide are estimated at \$ 1 trillion in 2010 surpassed. According to analysts, the demand for Islamic banking is growing in the background of the ongoing global financial crisis, as banking institutions, based on these principles, have demonstrated greater stability.

According to Islamic rules (Fiqh al-Muamalat), banks are prohibited from paying interest. There are currently Islamic banks operating in Muslim countries - Iran, Sudan, Malaysia, Bahrain, the Gulf and various parts of the world. Some economists thought they would go bankrupt even when they first worked on interest-free Islamic banks. However, during the global financial crisis, the growth of Islamic banks' bankruptcy instead of bankruptcy proves that their sustainability is stronger than other banks.

The first Islamic banks to compete with modern traditional banks emerged in Pakistan in the 1950s and 1960s. The rapid development of banks operating on the principles of Islamic banking increased interest in other Muslim countries as well. Banks operating under Islamic Sharia in Egypt and Malaysia in 1960 and in the Gulf countries, whose core capital is the oil money, began operating in the

1970s. Nearly 30 such banks have been operating in the last ten years of the last century.

In 1979, for the first time in the world, a state-owned bank operating in Pakistan was opened. This process continued until 1985. In July 1983, in Sudan, banks operating in the Islamic state were established in Sudan. In the Islamic Republic of Iran, the Islamic Revolution, after the fall of the Shah era, in March 1984 a draft of "Bank Laws" "The Islamic Bank of Iran" was created. In 1985, there were more than 50 Islamic banks operating in the world with Islamic principles.

The Islamic Financial Organization was established in Bahrain on February 26, 1990. It has already demonstrated Islamic banking in the world banking system. Then, in 1991, Indonesia's first Islamic bank, Muamalat Bank, was established. Nearly 2000 Nearly 200 Islamic Financial Institutions were established. 40% of them were in the East, 20% in African countries, and 40% in the US and European countries.

These Islamic banks are different from traditional banks .If Islamic banks are dominated by interest - earning assets in the formation of classic banks' revenues, Islamic banks are actively carrying out their operations and are actively involved in the performance of their responsibilities in the Islamic economy. Islamic banks, along with ordinary banks, have gained a stable position in their countries. The banks operating in the Islamic banking principles known as Private Finance Institutions are rapidly developing and rapidly developing.

In 2000, the Islamic Financial Services Department, working in international standards in Kuala Lumpur, Malaysia, was created, and the development of Islamic banking in the world resulted in a great deal of dissatisfaction. Many non-Muslim countries began studying the principles of these banks. The high rates of growth of Islamic banks over the past decade have been understood that such an economic model is an economic system relied on in the global economic system.

In September 2004, the first Islamic bank in the British capital, London, was set up, and these banks quickly began to compete with local banks. Islamic banks gained steady positions along with ordinary banks in their countries.

Currently, about 150 financial institutions operate on the basis of Islamic values or, more precisely, they turn it into a life credit. These financial institutions operate in non-Muslim countries such as the UK, the US, the Philippines, and Scandinavia (Denmark, Norway, etc.) a number of American and English banks (Citibank, UBS, HSBC, etc.) have set up specific divisions to serve customers in accordance with Islamic law. The total amount of funds managed by Islamic laws is about \$ 150 billion, according to expert estimates.

Despite the increasing influence of the financial crisis in America and the West, Islamic financial institutions and banking are rapidly evolving. It should be remembered that in recent days, the Vatican's official newspaper also said that the only way out of this crisis was Islamic banking. The main reason why Islamic banking has achieved great success in 2008 is that the commitments in the American and Western banks are tough and not serious. Although the development of banks in American and Western banks is based on credit interest rates, the banking sector is being developed in Islamic banking, not by these interest rates, but by investing.

One reason for his success in 2008 was that there is no interest on mortgage loans. The main reason for the financial crisis in the United States was that people could not afford the growing interest rates of mortgages. This resulted in a non-repayment of \$ 1.7 trillion in loans.

The Islamic economy and banking have gained noticeable growth since the 70s of the last century and now there is a steady development dynamics in this area. In the Islamic finance system, not only Islamic Finance Institutes, but also its contracting partners, which have a specific place in the market, are closely involved. In addition, many Muslim countries are transforming their economic and financial structures fully into Islamic finance principles. Now some CIS countries are also interested in projects implemented in Islamic finance business. Currently,

more than 80% of Islamic financial institutions fall to the Persian Gulf countries, more than 42% of their financial funds are in the Persian Gulf, South and Southeast Asia is concentrated.

The Islamic banking system definitely implements interest-free loans for the implementation of this or that project. At the same time, it participates in profits earned by financing foreign trade operations. Whether interest-free lending or interest-sharing is determined at the end of transactions. As a rule, banks finance more trade-related import-export operations. Here, the share of earnings by participating in the operation appears to be a profit, not interest. The difference between the Islamic banking classic banking system is related to the fact that it shares its share of profits at the end of the transactions. Thus, he can completely move away from the predetermined interest rate, riba and intention.

In addition, Islamic-based trading banks are also operating in Muslim countries. In general, the Islamic banking system can be divided into 3 groups:

1. Islamic Development Bank ;
2. Social-styled Islamic banks ;
3. Islamic Based Trade Banks .

Islamic banking differs in the banking sector of each country according to its organizational structure and activities and is divided into different forms:

- 1) Islamic banks in the government sector (Pakistan, Iran, Sudan);
- 2) Islamic banks operate in the mixed sector, namely traditional banking and Islamic banking (Turkey, Egypt, Jordan, Malaysia)
- 3) Non-bank financial institutions (Bangladesh, India)

Many large banks in the world have special departments to serve clients in accordance with Islamic rules. These banks are examples of:

1. Citibank
2. UBS
3. HSBC

4. Commerzbank
5. Europe Arab Bank Plc, London
6. Islamic Bank of Britain
7. ABS International Bank, London
8. BADR bank, Russia
9. Deutsche Bank and others.

The International Islamic Banking Association was established to ensure the economic and social development of the countries and to ensure the links between Islamic banks all over the world. International Islamic Banks Association (IBA) was established in 1978 by the initiative of Prince Mohammed al-Faisal al-Saud (Saudi Arabia) was established in Jeddah, the capital of Saudi Arabia. The purpose of the International Islamic Banks Association (IBA) is as follows:

- applying Islamic principles to banking;
- Technical assistance to national Islamic banks;
- joint preparation of new projects and projects;

International Islamic Banks Association includes:

- Islamic banks in Sudan;
- Bahrain's Islamic banks;
- Jordanian Islamic bank;
- Islamic banks in Iran;
- Faisal Islamic Bank (Egypt);
- Kuwait Finance House (Kuwait)

The Islamic Development Bank currently includes 56 member countries and member countries are steadily increasing. IDB member countries and their shareholding or membership fees are as follows (Amounts expressed in millions of Islamic dinars):

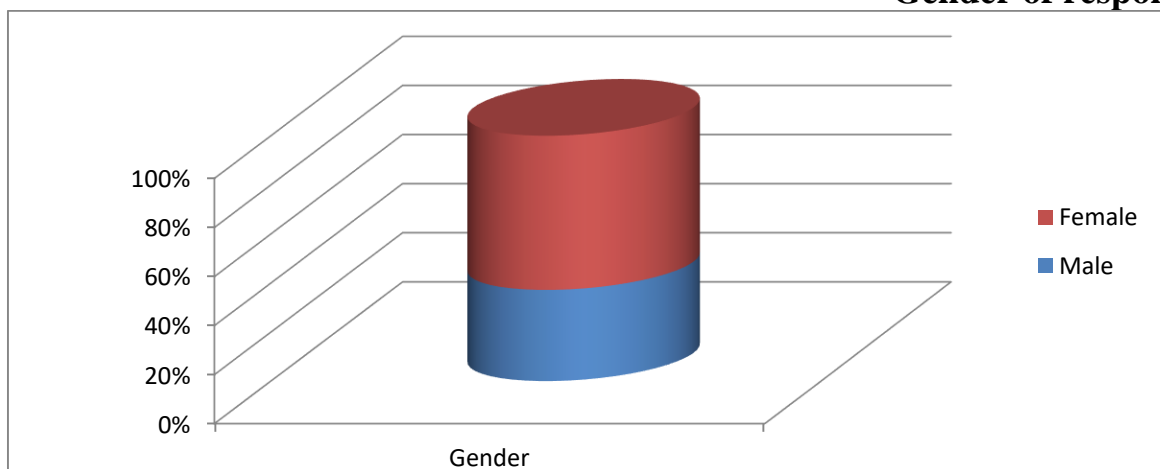
- 1) The Islamic Republic of Afghanistan - 9.93 (0.12% of the total)
- 2) Republic of Albania - 4.96 (0.06% of the total)
- 3) Algeria - 246.67 (2.88% of the total)
- 4) The Republic of Azerbaijan - 9.77 (0.11% of the total)

- 5) The Kingdom of Bahrain - 13.90 (0.16% of the total)
- 6) Bangladesh People's Republic - 182.17 (2.13 out of total)
- 7) Benin Republic - 9.77 (0.11% of the total)
- 8) Egyptian Arab Republic - 686.84 (8.01% of the total)
- 9) Republic of Indonesia - 406.49 (4.74% of total amount)
- 10) Islamic Republic of Iran - 694.51 (8.11% of total amount)
- 11) Malaysia - 157.93 (1.84% of the total amount)
- 12) Pakistan Islamic Republic - 459.21 (5.36% of the total amount)
- 13) Kingdom of Saudi Arabia - 1,979.74 (23.10% of the total amount)
- 14) The Republic of Turkey - 626.24 (7.31% of the total amount)
- 15) United Arab Emirates - 561.84 (5.56% of the total amount) and others.

3.3. Preparation of action plan for Islamic banking in Azerbaijan.

A survey was conducted in Azerbaijan as part of the research work to measure the population's interest-free banking awareness, the attitude of the society to the banking sector and the services offered by commercial banks and the interest of the population to interest-free banking services. The survey included 293 respondents with different age categories, employment levels, marital status and monthly income. Key information about respondents is as follows:

Figure 3.1.
Gender of respondents



37.2% of respondents are men and 62.7% are women. Only 16.3% of respondents are married. The survey participants were in the following age categories:

Table 3.2.
Age composition of respondents

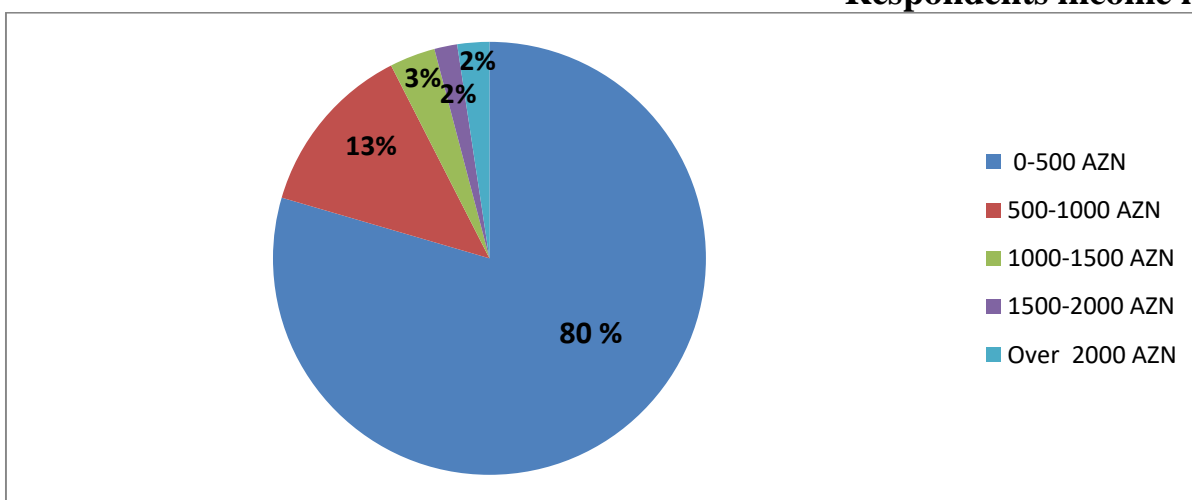
Age	Number of respondents	Percent
Between 18-24	209	71.3 %
Between 25-34	75	25.6 %
Between 35-44	7	2.4 %
Between 45-54	2	2 %
Over 55	0	0.68 %

According to the employment status of respondents, 25.2% work in the private sector, 15% in the public sector, and 10.2% are unemployed. Among the respondents, there were 144 students .The retired was not.

According to the respondents' education level, 204 people have higher education, 84 are incomplete higher education and 5 are secondary.

80% of respondents, ie monthly income of 233 people less than 500 AZN, 38 to 500-1000 AZN, 3% respondents earn monthly income of 1000-1500 AZN. There are 5 people who earn 1500-2000 AZN and 7 people who earn over 2000.

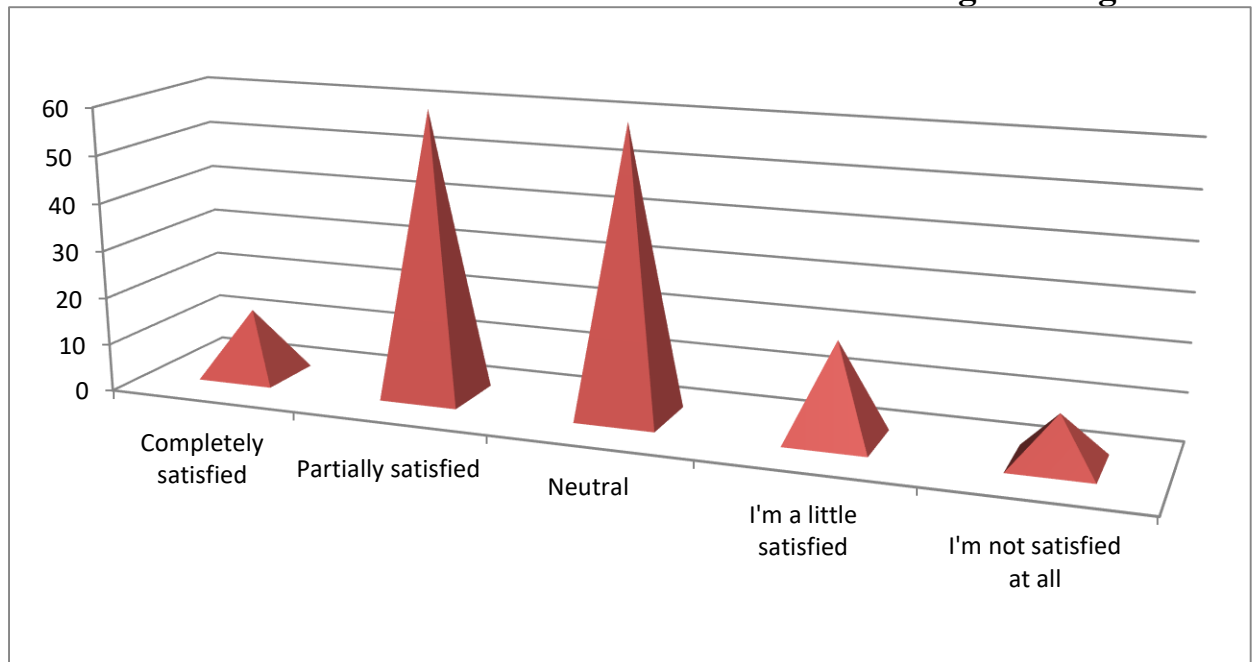
Table 3.3.
Respondents income level



Respondents' attitude to the traditional banking system

164 respondents (about 56%) use bank services. . These people use 40 credit cards, 17 deposit accounts and 48 credit card banking services. 59 respondents use multiple services of interest-bearing banks.

Figure 3.4.
Satisfaction with interest-bearing banking services

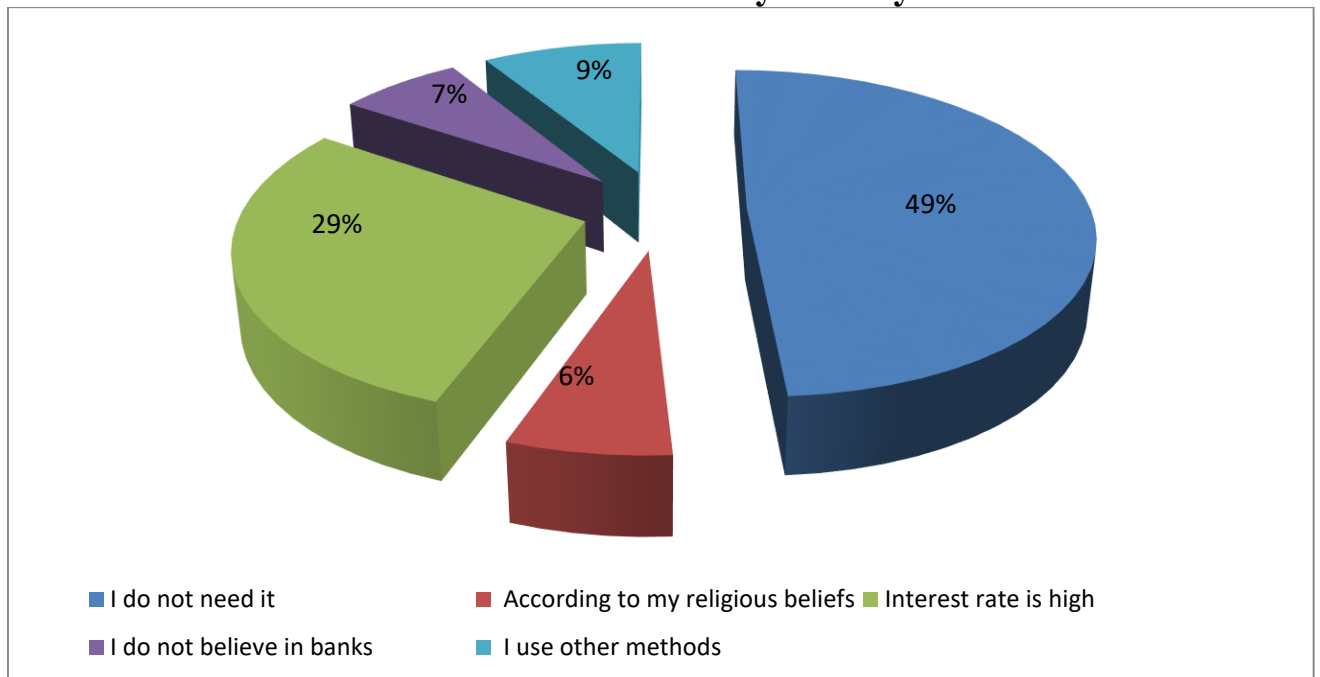


The satisfaction level of respondents using banking services can also be lower. Thus, only 8.5% of 164 respondents were satisfied, and 36.5% expressed partial satisfaction. 36.5%, ie 60 people, neutrally assessed the level of satisfaction with the banking services. 10 people were not completely satisfied.

On the other hand, low levels of satisfaction are observed in credit and credit card users. Thus, the ratio of those who use 55 credit services is very low. In other services, this indicator can be partly considered high.

The majority of respondents see the customer's immediate cash need, as the main advantage of banking services. The main reason for carrying out cashless operations and protecting customer deposits is also the main reason.

Figure 3.5.
Why do not you use bank services?



Out of 129 people who do not use commercial services, 49% said they did not need bank services and that 9% met their money needs in other ways. Contrary to expectations, the percentage of those who did not benefit from banking services was very low. 29% of the population noted high interest rates in the traditional banking system.

Respondents' attitude to banks acting on the principle of investment and trade

First of all, the attitude of the respondents to the investment and trade-oriented banks was measured. As a result most of the population noted that they were not sure about this. But at the same time it is thought that 120 banks can operate on the principle of investment and trade. 24 people said it was not possible.

About 148 people say they are not convinced that the Islamic banking system can compete with the traditional banking system.

Respondents' attitude to Islamic banking

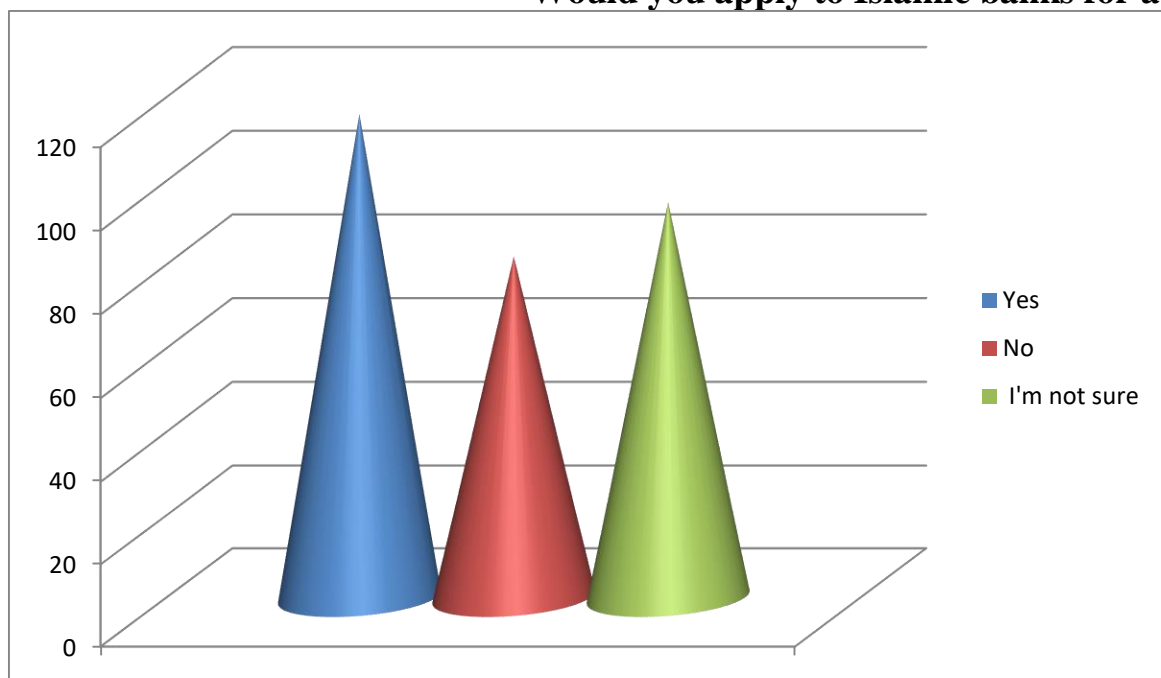
The majority of respondents answered the question "Do financial services of Islamic banks require a thorough analysis of customer risks and whether the state should ensure the operation of banks providing investment and trade-based financial services?" Most respondents "agree" and "yes". Of the respondents,

43.6% of respondents said that they agree with the idea that Islamic banks will have a more positive impact on the economy. 141 people said they would believe this opinion after examining international experience.

131 respondents noted that the Islamic banking system was legitimate by the state, and that 117 had difficulty in answering these banks.

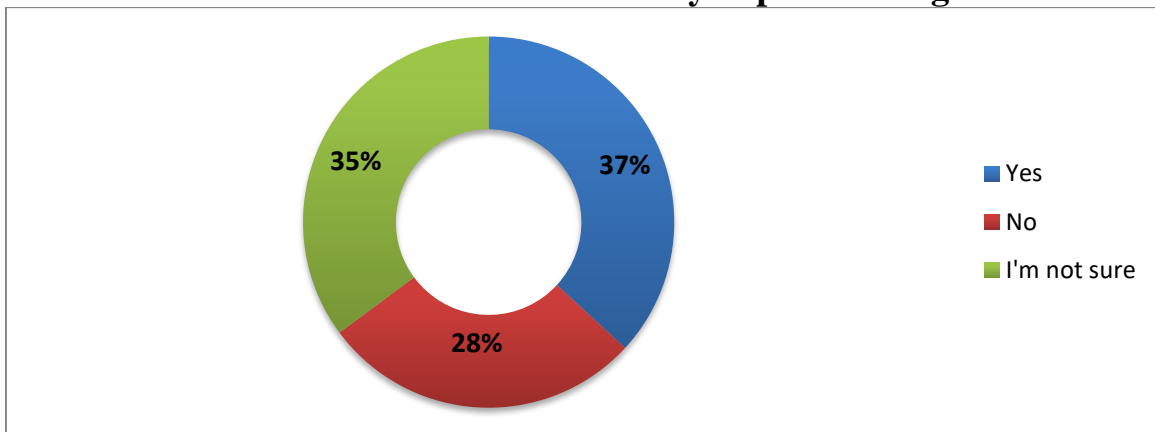
"Establishing an Islamic banking system will strengthen competition in the country's financial markets and traditional banks will be forced to lower their interest rates." A survey of the population was asked to express this opinion. As a result, 138 people were satisfied with the idea, 133 said they were not sure.

Figure 3.6.
Would you apply to Islamic banks for a loan?



As it is clear in the graph, 116 people in the survey agreed to apply to Islamic banks. Generally, the number of unstable and unwilling to use is very close to each other.

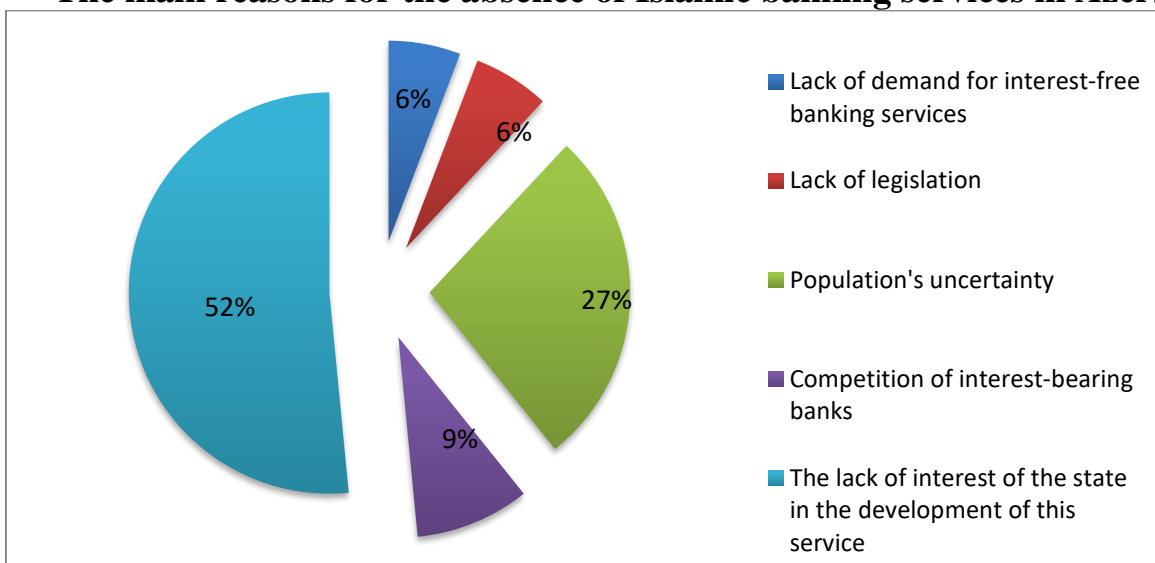
Figure 3.7.
Would you place savings in Islamic banks?



108 people said "yes" and 82 people answered "no", 103 said they were undecided.

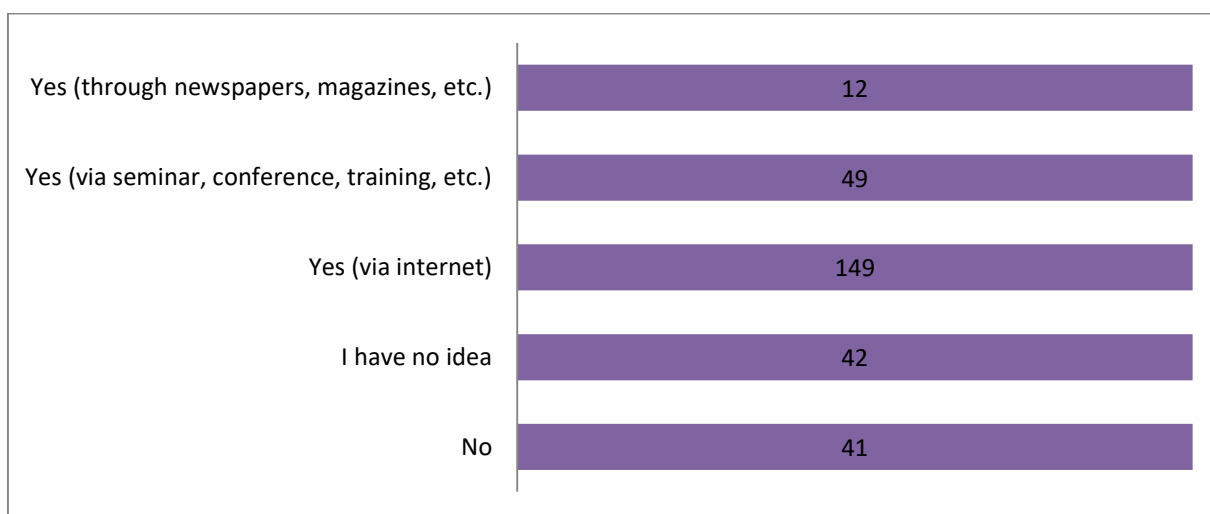
The survey also examined why the lack of interest-free banking system in Azerbaijan was investigated. These reasons were presented to respondents in 5 answers and the following result was obtained.

Figure 3.8.
The main reasons for the absence of Islamic banking services in Azerbaijan



Thus, the lack of interest-free banking services in Azerbaijan connects 6% with the vacancy in the human rights system, 9% compete with 27% interest rate banks, and 27% of the population's uncertainty. The number of those who answered the lack of interest-free banking services was 17 people. The survey showed that 151 states lacked the interest of the state in the development of this service.

Finally, people were asked if they wanted to get detailed information about Islamic banking. These 5 answers were presented to the respondents and the following result was obtained.



As a result of the research, the current situation of Islamic banking in Azerbaijan and around the world has been investigated and it has emerged that the following development problems exist:

- Legal arrangements and the existence of gaps in the legislative system,
- Specialist minority,
- The system is new and not fully integrated,
- The lack of institutions supporting interest-free banks,
- Lack of uniform market and accounting standards among Islamic banks

In order to measure the awareness of the population of Azerbaijan on the interest-free banking system, to determine the willingness to use these services and to identify existing problems, survey questionnaire was conducted within the framework of the research. The survey conducted among 293 respondents, who differed in age, employment, marital status and monthly income, identified the following significant results:

- Knowledge of the population with interest-free banking services and principles is relatively low,
- The degree of satisfaction of those who use services of interest-bearing banks (especially those who are lenders) is low,
- There is a lack of interest on banks' interest-free operation,

- Most respondents believe that the creation of interest-free banks will lead to the development of the economy and the banking system, as well as the fall in interest rates in other banks,
- The desire of the population to use interest-free banking services is high,
- The majority of respondents who received loans from interest-bearing banks stated their intention to use interest-free banking services in the future,
- The lack of interest-free banks is linked to the lack of interest of the state in the development of this service
- According to the respondents, if the state provides interest-free banks, the confidence in them will be higher

Based on the information obtained from the survey and survey, the following activities may be proposed:

1. Implementing regular measures related to the interest-free banking system, coverage of the issue with the media and media will serve to increase public awareness. According to the survey results, 50.8% of the respondents would like to receive this information via the Internet, 34% - through seminars, conferences and training, and in the smallest part - in newspapers, magazines and other publications.
2. It is important that the state encourages the establishment of non-interest-oriented banks, given the high demand for the population to use interest-free banking services.
3. The state should ensure the formation of a legislative system and the procurement regulations that will create the basis for the creation and development of interest-free banks.
4. It may be suggested that higher education institutions incorporate the interest-free banking system into the curriculum, conduct classes and create specialties in order to minimize the problem and eliminate the problem in the future.

Extensive research and surveys conducted in the Islamic banking sector have shown that there are enough customer segments in Azerbaijan who want to use Islamic banking products. These include halal manufacturing enterprises,

entrepreneurs who want to apply different financing techniques, and a country that does not use traditional banking products.

The Republic of Azerbaijan is the shareholder of the Islamic Development Bank since 1992. During this period, our country has implemented 61 projects with a total value of \$ 1.7 billion, and some of them are still being continued by the IIB and its institutions. The implemented projects are mainly economic projects and, in the end, serve to strengthen the economic potential of our country. These projects were made possible by the signed protocols and agreements between the Government of Azerbaijan and the IDB. These treaties and protocols are the legal basis for these projects and the source of the regulation.

At present, the relevant legislation is being drafted by the Ministry of Economy of the Republic of Azerbaijan in connection with gradual introduction of the Islamic Finance system in the Republic of Azerbaijan. The Islamic Development Bank has allocated \$ 200,000 (two hundred thousand) US dollars to the Government of Azerbaijan for these works. The funds include the selection of the consultant company, the analysis of the existing banking legislation and the development of a draft law in line with the economic policy of the country. The future application of the law envisages the creation of a dual financial system (traditional and Islamic) in the Republic of Azerbaijan.

Creating a legislative framework for the regulation of Islamic financial activity, making amendments and additions to the laws of the Republic of Azerbaijan on Property, Taxes and Customs, Banks and Banking Activities, Securities, Investment Funds, Deposit Insurance, State Real Estate Register, Accounting Laws and other legal acts or the adoption of a separate law "On Islamic Banking Activity".

The establishment of the Islamic financial system in the Republic of Azerbaijan will contribute to the formation of a better financial market by creating a highly competitive environment between traditional and Islamic banking systems. At the same time, the application of Islamic banking and the creation of a dual financial system will give the country the following benefits:

- Strengthening financial stability of the country
- Expansion of economic investment activity with the establishment of Islamic Banking
- Establishing Islamic insurance activities
- Developing Islamic capital and money market
- Strengthening the competitive environment in the domestic financial market
- Extensive cooperation with international Islamic financial institutions and attracting additional investments to the country
- Further expansion of economic and political relations with the Organization of Islamic Countries of Azerbaijan

CONCLUSIONS AND SUGGESTIONS

The vulnerability of the population to interest and religious principles resulted in the need to meet the investment needs of the economy in the Muslim countries by foreign borrowing and to increase the political and economic dependence of the state from foreign countries, despite the fact that the people had financial resources to support the country's development. Therefore, unlike traditional banks, there was a need to establish businesses offering services that meet specific Islamic rules. Examples of these guidelines include the prohibition of interest, the use of money as a trading tool, the distribution of risk between the parties, the non-interference in the market, the prohibition of all activities related to indefinite situations and merely the subject matter of Islamic law and activities for financial investment .

Nowadays, it is widely regarded as one of the fastest-growing sectors of interest-free banking in countries with financial markets like the United States and the United States, not just in Muslim countries, but also in the global financial market. The European and American countries are trying to attract oil-incomes in the Muslim countries by opening interest-free banks or departments.

Currently, Islamic banks operate in many countries around the world. Some countries have completely demoralized banking systems. Examples include Islamic Republic of Iran and Pakistan. In many countries, non-bank Islamic financial institutions are functioning. Some of them are:

- Australian Islamic Investment Company -Melburn;
- Nassau Islamic Investment Company - Bahamas;
- Bahrain Albaraka Islamic Investment Bank - Manama;
- International Islamic Bank of Denmark - Copenhagen;
- Egyptian Arab Investment Bank - Cairo;
- Luxembourg Islamic Finance House Universal holding;
- Swiss Islamic Investment Company - Geneva;
- Turkey Albaraka Turkish Finance House - Istanbul;
- Albaraka International Ltd, London;

- Al Rajhi Company for Islamic Investment - London;
- Islamic Finance House Public Ltd. - London.

However, Islamic banking has not been widely developed in the CIS as well as the advantages of economic agents formed throughout history as well as the lack of awareness of customers, bankers and state authorities about the Islamic financial system. Significant changes in Azerbaijan's economy continue: deep and necessary reforms have taken place from macro and micro-economic management systems to all aspects of modern finance and credit policy. The modern banking system of the Republic of Azerbaijan and its management, organization and use of banking resources, banking management and marketing are of particular relevance today.

Problems with the development of interest-free banks are mainly due to the lack of them. The lack of financial instruments, the inability to meet urgent financial needs, the failure to finance long-term projects, non-participation in government funding, the lack of access to monetary markets, the inability to use credit for the document and competing with interest-bearing banks were identified as the missing sides of interest-free banks. In addition to these problems, interest-free banks may be criticized for some features:

- The fact that the interest rate and interest rates do not exceed each other,
- Non-interest-free banks do not use media frequently,
- Only targeted target audience,
- Uncertainty as a result of poor system submission,
- The similarity of procedures to traditional banks,
- The idea of making credit card applications wrong.

There is currently a customer segment of Islamic banking in Azerbaijan and, first of all, depends on the following factors:

- The majority of Azerbaijan's population is Muslim;
- There are many investment-oriented areas in Azerbaijan, and there are many opportunities for the development of Islamic banking in Azerbaijan.

Azerbaijan has the potential to become a regional center of Islamic banking. The emergence of Islamic financial institutions in the country where there are quite a few Muslim entrepreneurs, who are not yet ready to rely on their traditional money to traditional banks, nor use traditional bank services, will increase the effectiveness of the financial market and speed up its development.

It should be noted that before making a decision on stimulating the development of Islamic financial institutions in Azerbaijan, it is necessary to carefully consider all the consequences of this step. Thus, it should be considered that the emergence of Islamic financial services can not lead consumers who did not use financial services to the financial sector, but rather to attract more consumers from Islamic financial institutions to ordinary financial institutions.

Azerbaijan is still at the stage of the establishment of Islamic financial institutions. The future will show how successful the development will be. At the same time, we consider that there is no need to accelerate this process. In other words, the creation of Islamic financial institutions in Azerbaijan is only possible when economic agents' demand for such financial services is considerably increased.

It is difficult to realize and rapidly develop Islamic Banking in the rapidly developing classic banking system in Azerbaijan. According to Article 33 of the AR Law on Banks, no bank is engaged in wholesale or retail trade, manufacturing, transportation, agriculture, development of fields, construction and insurance activities, or excluding insurance organizations, partner, associate or shareholder as such. The Bank may only engage in the sale of merchandise, partnerships or other legal entities engaged in the activities of wholesale or retail trade, manufacturing, transportation, agriculture, development, construction and insurance activities, with the permission of the financial market supervisory authority, or the shareholder may participate.

However, there are broad prospects for achieving the development of this system in Azerbaijan, and these perspectives are to be considered and explored. As you know, our credit interest rates are quite high in our country. Of course, taking

credit under these conditions also leads to problems. For this reason, it is desirable to have a large number of Islamic banking banks in our country. Therefore, taking the next key steps to develop Islamic Banking can be considered as a very competitive one:

- First of all, the main principles of functioning of Islamic Banking should be clarified, the realities of the Azerbaijani society should be taken into account and the delivery mechanisms should be identified;
- The Central Bank and Financial Market Supervisory Authority in the field of research, policy papers, financing and implementation of such projects across the country between economic and social organizations and reviewing strategic papers;
- Initially, "pilot tools" should be analyzed and tested;
- Preparation and submission by the Central Bank of the Republic of Azerbaijan and Financial Market Supervisory Authority of the executive document to regulate this system
- Rules for possible adjustment and effective implementation of all transactions should be developed;
- As with traditional banks, this banking system should also provide high level of customer service and service.

On January 18, 2017, the grant agreement was signed between the Government of the Republic of Azerbaijan and the Islamic Development Bank on technical support for the development of the legal framework for Islamic financing in the Republic of Azerbaijan. According to the document, it is envisaged to analyze existing legislation in the field of banking in Azerbaijan, to study the possibilities of applying Islamic banking in our country and prepare relevant proposals.

If Islamic banking is fully functioning in Azerbaijan, it will be possible to attract such investors from Arab countries, primarily from Saudi Arabia, the United Arab Emirates, Qatar, as well as from other Muslim countries, including Turkey

and even from Iran. They have the opportunity to bring these countries to Europe and the CIS through Azerbaijan.

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ADDITIONS
QUESTIONNAIRE

**"INFORMATION LEVEL OF POPULATION OF ISLAMIC BANKING IN
AZERBAIJAN"**

- 1) What is your gender?
 - a) Male
 - b) Female
- 2) Please write down your age.
 - a) between 18 and 24
 - b) between 25 and 34
 - c) between 35 and 44
 - d) between 45 and 54
 - e) over 55 years old
- 3) What is your marital status?
 - a) Single
 - b) Married
- 4) What is your education level?
 - a) high education
 - b) incomplete higher education
 - c) secondary education
- 5) Do you work?
 - a) I work in the private sector.
 - b) I work in the public sector.
 - c) Retired.
 - d) I am a student.
 - e) I am unemployed
- 6) What is your income ?
 - a) 0-500 AZN
 - b) 500-1000 AZN
 - c) 1000-1500 AZN

- d) 1500-2000 AZN
 - e) Over 2000 AZN
- 7) Do you use services of traditional banks?
- a) Yes, I use it.
 - b) No, I do not use it.
- 8) Which banking services do you use?
- a) Credit
 - b) Deposit
 - c) Credit card
 - d) Money transfers
 - e) None
- 9) Are you satisfied with the services of traditional banks (if you use them)
- a) Completely satisfied.
 - b) Partially satisfied.
 - c) Neutral
 - d) I'm a little satisfied.
 - e) I'm not satisfied at all.
- 10) For what reason do not you use interest-based banking services? (If you do not use it)
- a) I do not need it
 - b) According to my religious beliefs
 - c) Interest rate is high
 - d) I do not believe in banks
 - e) I use other methods
- 11) What do you think as the main reason why people use bank services?
- a) Citizens' need for money
 - b) Non-cash payments
 - c) Saving of customer deposits with debit accounts
 - d) Business financing
 - e) Other

- 12) In your opinion, can banks operate in Azerbaijan on the basis of trade and investment principles?
- a) Yes
 - b) No
 - c) I'm not sure
- 13) In your opinion, the Islamic banking system can compete with the traditional banking system?
- a) Yes
 - b) No
 - c) I do not know about this
- 14) Financial services of Islamic banks require more detailed analysis of customer risks. What do you think of it?
- a) I do not agree
 - b) I agree
 - c) I do not know
- 15) Do you think the state should provide banks with investment and trade-based financial services?
- a) Yes
 - b) No
 - c) I'm not sure
- 16) Investment and trading-based banks have a bigger impact on the economy. What do you think of it?
- a) I do not agree
 - b) I agree
 - c) I have to study international practice
- 17) If the Islamic banking system is legally governed by the state, do you trust these banks?
- a) Yes
 - b) No
 - c) It's difficult to answer for me

- 18) Establishment of Islamic banking system will strengthen competition in the financial market of the country and traditional banks will be forced to lower interest rates. What do you think of it?
- a) I do not agree
 - b) I agree
 - c) I'm not sure
- 19) If Islamic banks are established, would you apply to these banks for loans?
- a) Yes
 - b) No
 - c) I'm not sure
- 20) Would you place savings in Islamic banks?
- a) Yes
 - b) No
 - c) I'm not sure
- 21) What is the main reason why there are no Islamic banking services in Azerbaijan? (European countries, Turkey, Kazakhstan and Tajikistan are already operating such banks).
- a) Lack of demand for interest-free banking services
 - b) Lack of legislation
 - c) Population's uncertainty
 - d) Competition of interest-bearing banks
 - e) The lack of interest of the state in the development of this service
- 22) Would you like to know more about Islamic banking
- a) No
 - b) I have no idea
 - c) Yes (via internet)
 - d) Yes (via seminar, conference, training, etc.)
 - e) Yes (through newspapers, magazines, etc.)