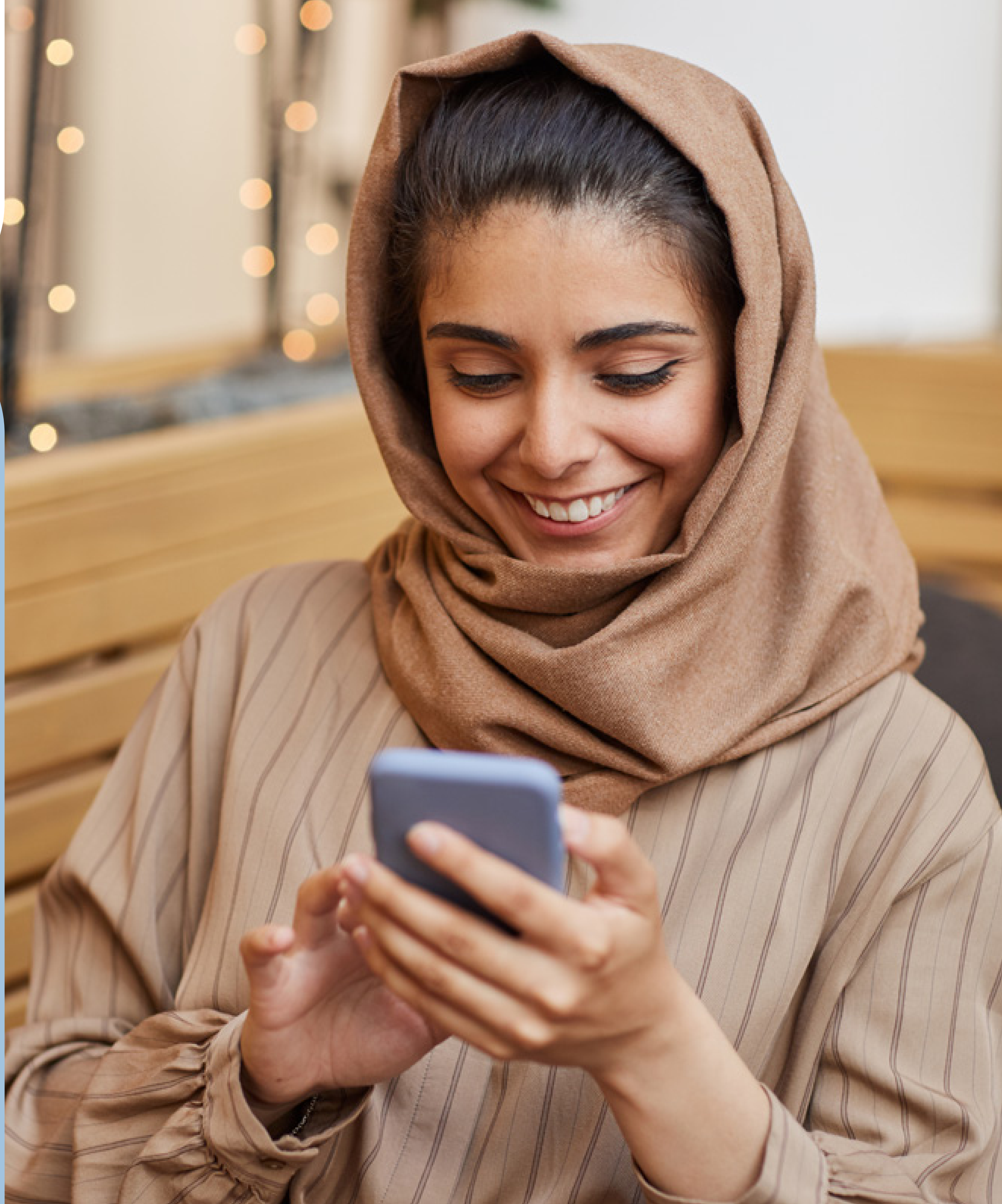
The ultimate guide to Islamic Banking

How ethical finance is shaping the future of banking



The opportunity

Islamic banking is entering a transformative new chapter. Long centred in Muslim-majority countries, it is now expanding globally - fuelled by digital innovation and the rising demand for more ethical, transparent, and inclusive financial services. This momentum is not only driven by devout Muslims but also by a new socially conscious generation of consumers - particularly Gen Z and millennials - who want their financial choices, and banks, to reflect their values.

For this values-driven segment, Islamic banking's core principles of fairness, shared risk, and ethical investment resonate strongly. It's a model inherently aligned with environmental, social, and governance (ESG) priorities – helping institutions meet regulatory benchmarks while deepening trust and emotional connection with their customers. Recognising this, conventional banks are increasingly exploring Islamic banking as a way to diversify their offerings, tap into underserved markets, and align with the global shift toward purpose-driven finance.

The scale of the opportunity is hard to ignore: over 800 million Muslims remain unbanked, and Islamic banking assets are expected to exceed $6.7 trillion by 2027. While the industry currently spans more than 80 countries, nearly 95% of Shari'ah-compliant assets are concentrated in just 10, mostly in the Middle East. This reveals an enormous untapped market - particularly across Asia, Africa, and Europe:

- Asia, home to over 60% of the world's Muslim population, is leading the charge. The Asia-Pacific region already accounts for a quarter of global Islamic banking, with Malaysia, Pakistan, Bangladesh, and Brunei at the forefront, while Indonesia, the largest Muslim-majority country, is laying regulatory groundwork to scale rapidly through central bank initiatives
- Africa is emerging as another high-potential region. In North Africa, where over 90% of the population is Muslim, Islamic banking remains underpenetrated. While Nigeria has already built a $2.9 billion non-interest banking sector, interest is also surging in Egypt, Morocco, South Africa, Sudan, and Senegal
- Europe is an increasingly relevant frontier. With growing Muslim populations and a rising appetite for ethical finance, countries like the UK, Germany, and France are seeing heightened demand for Shari'ah-compliant offerings

Islamic banking is no longer just a niche - it's a strategic path to inclusion, relevance, and long-term growth. For banks seeking to expand their footprint and serve a values-driven generation of customers, now is the time to act.

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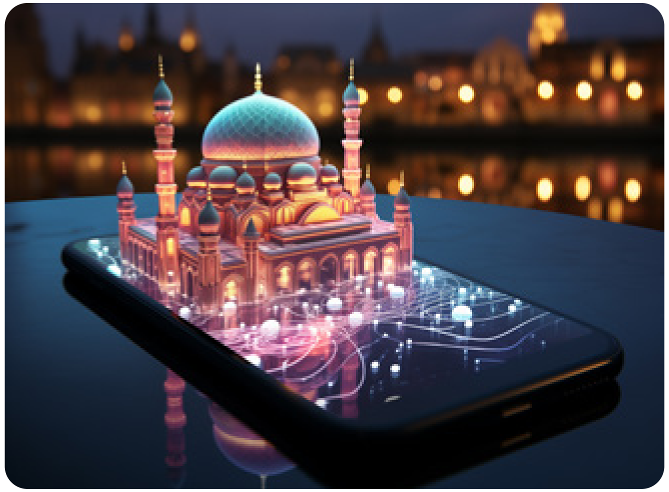
> Algbra & LSEG



Principles of Islamic Banking

Islamic banking is built on a distinct set of ethical and financial principles that set it apart from conventional models. Rooted in Shari'ah law, it offers a transparent, responsible approach to finance - one that emphasises partnership, shared risk, and real economic value.

Key principles include:

- No interest (Riba): Charging or paying interest is forbidden. Instead, returns come from genuine trade, leasing, or joint ventures
- Asset-backed financing: Transactions must be linked to tangible assets or services, avoiding speculative or uncertain deals
- Risk sharing: Profit and loss are shared fairly between parties, promoting partnership and discouraging exploitation
- Ethical investment: Investments avoid sectors like gambling, alcohol, and weapons, aligning finance with moral and social values
- Transparency: Clear, upfront disclosure of terms and costs ensures trust and accountability
- Social justice: Supporting financial inclusion and equitable wealth distribution is a key objective

These principles not only serve religious compliance but also resonate with the growing global demand for ethical, sustainable, and socially responsible finance - expanding Islamic banking's appeal beyond Muslim customers to a diverse, values-driven audience.

The appeal

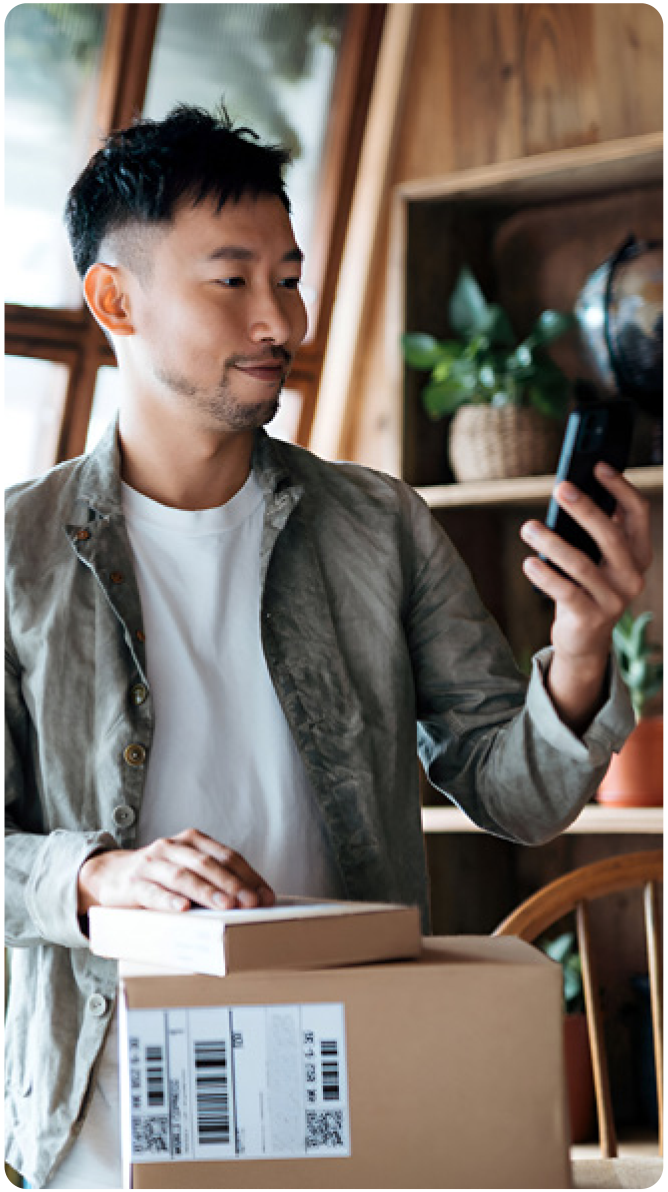
Why customers care:

- A banking experience that aligns with their values - religious or ethical
- No interest, no hidden fees
- Ethical investments that avoid gambling, alcohol, weapons, and other restricted areas
- Fair risk-sharing models
- Increasing access to digital-first Islamic financial products
- A fast-growing global movement aligned with trust and transparency

Why FIs should care:

- Reach underbanked and underserved Muslim populations
- Attract values-driven consumers seeking ethical finance
- Conventional banks can differentiate in saturated and commoditised markets
- High growth potential in Asia, Africa, and Europe
- Align with ESG and CSR goals
- Build long-term loyalty through value-based offerings

The starting point



For banks, the most effective way to enter the Islamic banking space isn't by overhauling their entire infrastructure - it's by launching a single, compliant product that can open the door to long-term market leadership.

Banks don't need to build full subsidiaries or Islamic windows from day one. Many start small, with one product designed to meet demand in a specific segment or geography, then scale up based on customer traction and operational readiness.

This phased, product-led approach allows institutions to:

- Build internal knowledge and confidence
- Demonstrate demand and impact
- Engage Shari'ah boards early without overcommitting

It's about learning by doing - and growing as you go. You don't have to change everything. Just start.

A good starting point is to focus on one of a few proven, Shari'ah-compliant product types. Broadly speaking, these offerings fall under two key Islamic banking models:

- **The service-based model** is built on fixed fees for services rendered. It supports a range of payments and card products - such as Ujrah cards, prepaid cards, and charity (Tabarru') cards - and is often the simplest to implement operationally.
- **The cost-plus model** is primarily used for credit products. It involves a predefined profit margin agreed upon upfront, as seen in structures like Murabaha, and is commonly used for instalment-based offerings such as Buy Now Pay Later (BNPL).

Here are four example products banks can use to take the first step:

- Ujrah card
- Charity card (Tabarru')
- Murabaha card
- Buy Now Pay Later (BNPL)

The four products:

Urjah Card (Fee-for-service)

Flat-fee, Shari'ah-compliant spending

What it is

The Urjah card is a Shari'ah-compliant payment product designed around a service-based model. It replaces interest with a clearly disclosed, fixed monthly fee - offering users a transparent, ethical alternative to conventional credit cards.

How it works

Rather than accruing interest, customers pay a flat fee for access to card services. Balances must be repaid in full each month, avoiding the risk of debt accumulation. This structure supports financial responsibility while ensuring full compliance with Islamic principles. Late fees, if applied, are symbolic deterrents and are donated entirely to charity, reinforcing the product's ethical foundation.

Delivery options

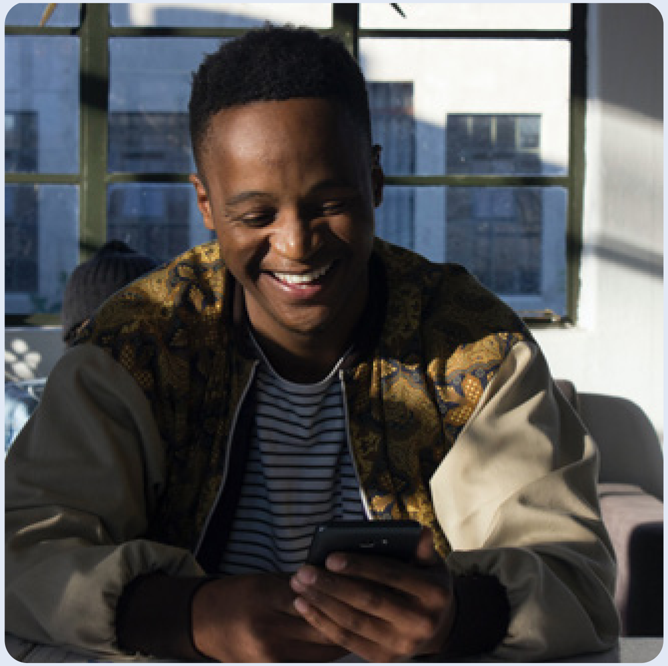
The simplicity of the Urjah model and the fact it can delivered through both physical and digital channels makes it ideal for digital banks, mobile wallets, and fintechs entering Islamic finance. It can be deployed quickly, making it a strategic entry point for institutions seeking fast, market access.

Why it works

Easy to explain and straightforward to manage, the Urjah Card builds trust with new customers - especially in markets where concerns about riba and hidden fees have previously limited card adoption. Its ethical foundation and operational simplicity make it a low-barrier, high-impact starting point.

Best for

- Traditional and digital-first banks looking to enter Islamic finance quickly
- Early-stage Islamic finance rollouts
- Customers seeking simple, ethical alternatives to conventional credit cards



Charity Card (Tabarru')

Purpose-led, Shari'ah-compliant giving

What it is

The Charity card is a values-aligned enhancement built on the Islamic principle of Tabarru' - voluntary giving. Added to Shari'ah-compliant financial products such as the Ujrah card, it enables customers to support approved charitable causes as part of their everyday transactions.

How it works

A fixed amount or small percentage of each transaction is donated to approved charities. Donations may be funded by the issuer, the customer, or shared between both. The mechanism is fully transparent, and customers can often choose the causes they wish to support.

Delivery options

The Charity card is a sub-product of the Urjah card and, as such, can be integrated well with digital banking apps and neobank platforms, enabling real-time impact tracking and customer engagement.

Why it works

The Charity card resonates strongly with socially conscious users - especially Gen Z and millennial segments - who want their financial choices to reflect their values. It enhances an institution's ESG profile and deepens emotional connection with the brand.

Best for

- Traditional and digital banks with strong CSR or ESG commitments
- Ethical fintechs and digital-first institutions enhancing social impact
- Socially conscious, impact-oriented customer segment

Murabaha Card (Cost-plus-sale)

Fixed-margin, Shari'ah-compliant credit

What it is

The Murabaha card offers a Shari'ah-compliant alternative to traditional credit, structured as a one-time, fixed-profit sale contract rather than interest-based borrowing. Based on the classical cost-plus model, it provides users with access to funds through a transparent, pre-agreed transaction that avoids riba entirely.

How it works

When a customer initiates a transaction, the bank purchases a commodity on their behalf, sells it to them at a pre-agreed profit margin, and immediately resells it as their agent, crediting the proceeds to the card balance. The customer then repays the marked-up amount in fixed instalments over time, with no interest or compounding. All terms are agreed upfront, and the process is repeated with each new usage, ensuring every transaction is tied to a real, underlying asset. Any late fees are symbolic and donated to charity, maintaining full Shari'ah compliance.

Delivery options

Ideal for issuers with experience in structured credit products, the Murabaha card can be delivered through both physical and digital channels. Early repayment incentives and spend controls can be layered in, helping institutions tailor offerings to specific user segments.

Why it works

The Murabaha card provides customers with flexible access to credit without compromising religious or ethical standards. It's particularly appealing to consumers who have previously avoided credit products due to concerns about interest, while still offering familiar functionality. It's one of the most widely approved structures by Islamic scholars and regulators, making it suitable for conservative markets.

Best for

- Institutions ready to scale or launch their credit offerings
- Consumers seeking instalment-based, interest-free credit
- Markets with unmet demand for Shari'ah-compliant credit services

Shari'ah-compliant BNPL

Interest-free, Shari'ah-compliant instalment finance

What it is

Shari'ah-compliant Buy Now Pay Later (BNPL) is an ethical alternative to traditional consumer finance. It avoids riba (interest) by using fixed, pre-agreed fees and transparent terms, ensuring full alignment with Islamic principles. Designed for Muslim and values-driven consumers, it provides flexibility without compromising financial ethics.

How it works

BNPL models vary in structure but share key features: no interest, fixed fees, and clear terms. All transactions are backed by actual goods or services, ensuring Shari'ah compliance.

At-purchase BNPL (off-card)

Customers pay using their preferred method at checkout but can convert eligible purchases into instalments on the spot. Merchants receive payment upfront (minus a fee), while the financial institution collects fixed-fee instalments from the consumer. Optional controls can restrict usage to Shari'ah-compliant products or accounts.

Best for e-commerce and in-store point-of-sale integration.

Post-purchase BNPL

After making a purchase, customers can opt to split payments into equal, fixed-fee instalments. There's no interest, and terms are fully disclosed upfront. This model offers users flexible budgeting while maintaining ethical transparency.

Ideal for digital banking apps offering spending flexibility.

Card-linked BNPL

Instalment options are embedded directly into Shari'ah-compliant credit or debit cards. Consumers can select interest-free instalment plans per transaction, with a flat fee based on amount or duration.

Seamless for institutions already offering Islamic card products.

Merchant-funded BNPL

Merchants offer customers 0% interest instalments, covering the cost via a flat fee paid to the BNPL provider. The merchant receives full payment upfront and the provider collects instalments from the customer.

Strategic for merchants entering the ethical or Islamic finance space.

Delivery options

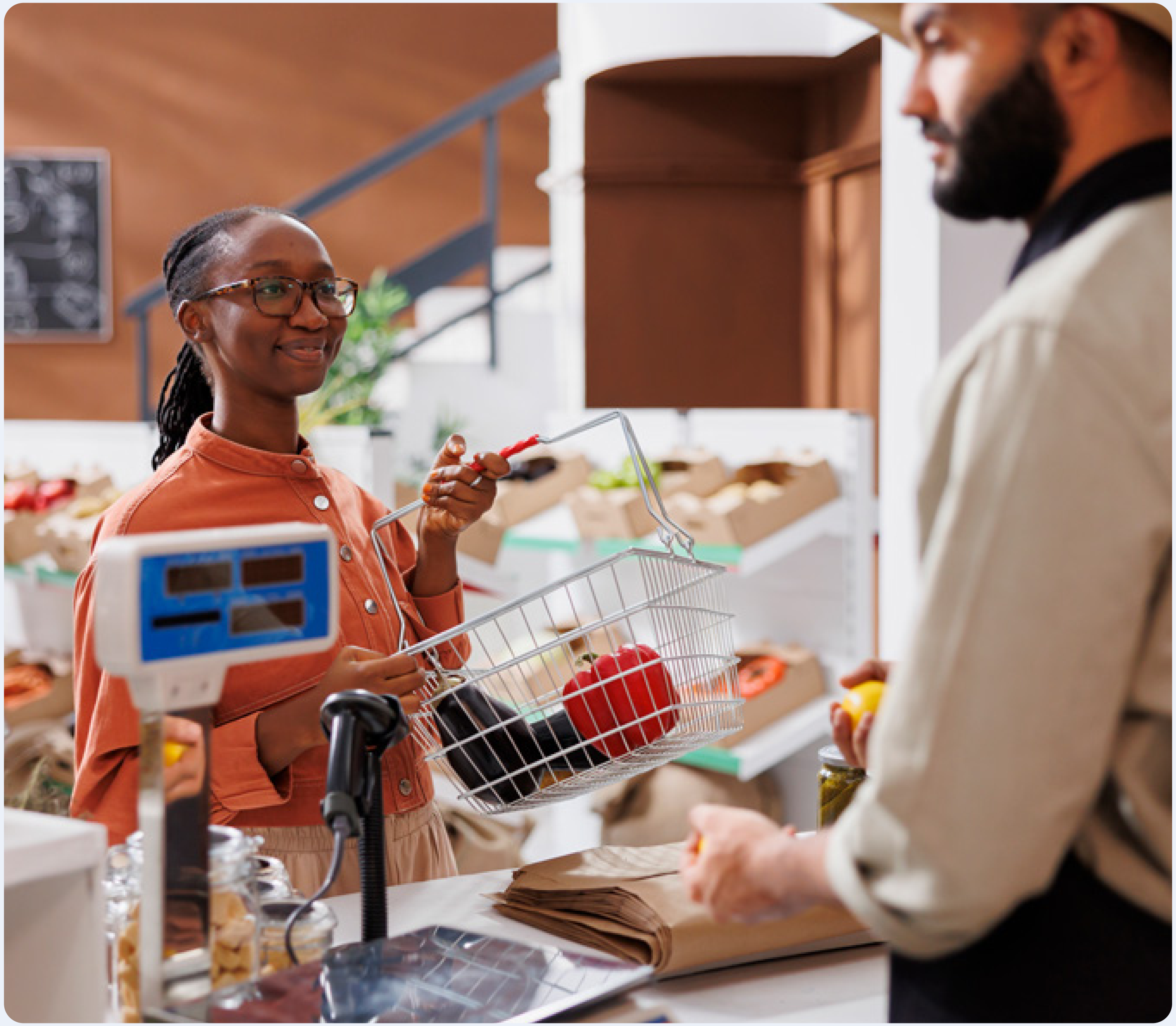
BNPL can be integrated into digital wallets, e-commerce checkouts, mobile apps, or physical point-of-sale systems. Its modular design makes it suitable for fintechs, digital-first banks, and merchants looking to expand ethical offerings.

Why it works

Shari’ah-compliant BNPL addresses growing consumer demand for transparent, ethical credit. It offers a compliant path to flexibility for users, while enabling institutions to differentiate, engage new segments, and align with values-based finance.

Best for

- Banks (traditional and digital) and fintechs launching or expanding Shari’ah-compliant consumer credit products
- Merchants interested in offering ethical, interest-free instalment checkout options
- Consumers seeking flexible, transparent, and Shari’ah-compliant payment plans



Shari’ah-compliant BNPL

The takeaways

The surge in demand for ethical banking - particularly Islamic Banking - presents a timely, high-growth opportunity for financial institutions to enter an underserved market and establish a competitive edge.

Islamic banking is booming - and the opportunity is huge

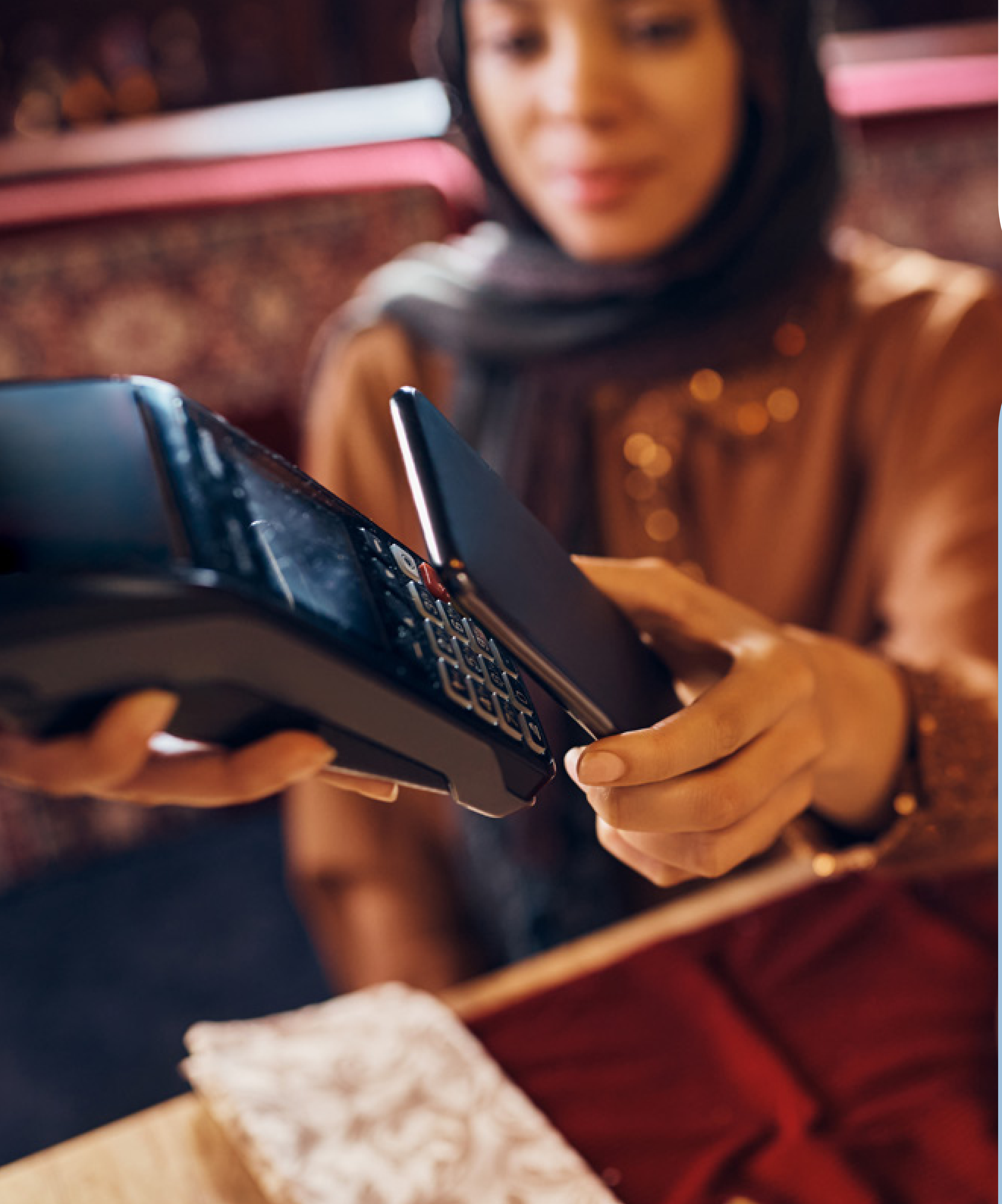
The market is expanding fast, driven by both Muslim and values-conscious consumers, making now the time for financial institutions to enter and lead.

Start simple, start smart

Launching a single Shari'ah-compliant product is enough to begin exploring the market. You don't need a full overhaul - iterating and evolving your offering over time depending on demand you see is the best way forward.

Choose partners wisely

If you're a bank looking to enter the Islamic banking space, it's important to select a partner that can simplify your technology landscape. Look for a vendor that offers the flexibility to support both conventional and Islamic banking services on a single, unified platform.



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