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SUPPORTING SMALL BUSINESS IN UZBEKISTAN THROUGH TRADITIONAL AND ISLAMIC FINANCIAL INSTRUMENTS

Senior Lecturer: **Orif Shakirovich Maksudov**, SamIES,
Azimshox Yunusovich Saidov
Student, Samarkand Institute of Economics and Service
Faculty of Banking and Auditing Group BI-S-221

Abstract. This research article examines the current state and development prospects of the financial support system for small and medium-sized businesses in the Republic of Uzbekistan. The author focuses on the synergistic effect of the parallel use of traditional bank lending, lines of international financial institutions, and new Islamic finance instruments implemented through microfinance organizations. The paper provides a detailed analysis of the legal framework, economic essence, and barriers to the integration of these two different financial systems in the context of macroeconomic reforms.

Keywords: small business, traditional banking system, Islamic finance, microfinance organizations, international.

Introduction. Small and medium-sized businesses are recognized worldwide as a key driver of economic growth, innovation, and employment. In the Republic of Uzbekistan, the development of this sector has been elevated to the level of a national strategic objective, as small businesses account for more than half of the country's gross domestic product and approximately 80 percent of all employment in the economy. Given the large-scale modernization and market liberalization undertaken in recent years, domestic entrepreneurs are facing the pressing need for high-quality and accessible financing.

Historically, the traditional banking sector has served as the primary source of borrowed capital for small businesses. However, high interest rates, strict collateral requirements, and inflation risks pose significant obstacles for aspiring and existing entrepreneurs. Alternative and complementary mechanisms today include resources from international financial institutions, as well as the rapidly developing Islamic financial services sector, implemented through microfinance organizations. The combination and harmonious development of traditional and Islamic financial instruments opens new horizons for stimulating business activity in the country. Currently, the institutional structure of Uzbekistan's financial market is characterized by the dominance of commercial banks. Traditional financial instruments for supporting small businesses include standard working capital loans, long-term investment loans for production modernization, financial leasing, project financing, and bank guarantees.

At the same time, the Central Bank of the Republic of Uzbekistan's base rate and the current inflation rate directly impact the market value of banking products. Average interest rates on commercial loans in national currency remain sufficiently high to ensure the stable development of long-term small business projects. In this regard, cooperation with international financial institutions such as the World Bank, the Asian Development Bank, the European Bank for Reconstruction and Development, and the International Finance Corporation is crucial.

International financial institutions provide targeted credit lines to commercial banks in Uzbekistan for subsequent refinancing to the small business sector. These funds typically have lower interest rates and longer repayment terms, reducing the financial burden on the end borrower. The state, in turn, through a specialized Entrepreneurship Development Company, is implementing

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mechanisms for partial guarantees and partial compensation of interest expenses on loans, significantly increasing the availability of traditional capital.

Along with the development of traditional mechanisms, a strong demand for alternative financial services based on the principles of ethical and Islamic banking is emerging in Uzbekistan. A significant portion of the economically active population and potential entrepreneurs in the country, due to their religious and ethical beliefs, completely reject traditional bank loans due to the presence of interest, which is classified as riba and strictly prohibited in Islamic law. A significant historical step in establishing the legal framework for this industry was the adoption of the Law of the Republic of Uzbekistan "On Non-Banking Credit Organizations and Microfinance Activities" in April 2022. This legal act officially granted microfinance organizations the right to provide Islamic finance services. The microfinance sector was chosen as a launchpad for piloting Islamic financial instruments due to its high flexibility, rapid adaptation to the needs of microbusinesses, and the absence of systemic risks inherent in large commercial banks.

Among the key Islamic financial instruments being implemented today by domestic microfinance organizations, the Murabaha agreement, which involves the sale of goods in installments with a pre-agreed markup, occupies a special place. Under this mechanism, a microfinance organization, on behalf of an entrepreneur, purchases the necessary equipment, raw materials, or vehicles from a third party and resells them to the client at a markup, with payment made in installments over a specified period. Also actively developing are Ijara instruments, which function as an analogue of traditional leasing, and Mudaraba, a partnership agreement where one party provides capital and the entrepreneur contributes their labor and management skills, sharing the resulting profits in an agreed proportion.

When examining traditional and Islamic financial instruments as a holistic system for supporting small businesses, it is necessary to clearly understand their fundamental economic differences, expressed solely through textual analysis. Traditional credit is based on the concept of lending money at interest, where the money itself is a commodity. In this model, the bank bears no commercial risks associated with the entrepreneur's activities, and all liability and risk of loss falls directly on the borrower. Even in the event of business bankruptcy, the obligation to repay the principal and accrued interest remains.

Conclusion. In summary, the study concludes that diversifying financial support instruments for small businesses through the simultaneous development of traditional bank loans, international lines of credit, and Islamic microfinance services is a strategically sound step for the economy of the Republic of Uzbekistan. The traditional sector provides the economy with significant resources for industrial and technological development, while Islamic microfinance addresses critical social issues, ensuring the inclusion of broad segments of the population in the formal economy, reducing poverty, and stimulating self-employment.

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