

Sharia-compliant financing as fiscal policy instrument: an Islamic economic approach to budget deficit management

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Abstract

Budget deficits are a recurring fiscal challenge for many countries, including Indonesia, where reliance on conventional financing methods such as interest-based debt often imposes long-term economic burdens. This study explores the potential of Islamic financial instruments as an alternative solution to address budget deficits, emphasizing sustainability, fairness, and compliance with sharia principles. Using a qualitative approach through literature review and descriptive analysis, the research examines the implementation and effectiveness of instruments such as sukuk, crowdfunding, and securities crowdfunding based on sukuk. The findings reveal that these sharia-compliant tools not only provide viable financing options without the burden of interest but also foster public participation and uphold social justice principles. The study highlights the importance of strengthening regulatory frameworks and integrating Islamic financial systems into national fiscal policies to create a more inclusive, stable, and ethical financing ecosystem. The implications of this research underscore the potential of Islamic finance to contribute to sustainable economic development while adhering to ethical and religious values.

Keywords: budget deficit, Islamic finance; sukuk; crowdfunding; sharia-based securities crowdfunding.

Introduction

Indonesia's economic growth is significantly influenced by various macroeconomic factors, including the Industrial Production Index (IPI), inflation, exchange rates, international trade, and Foreign Direct Investment (FDI). Industrial output and FDI serve as key drivers of growth, in line with both conventional economic frameworks and Islamic welfare principles. While controlled inflation can stimulate economic activity, trade deficits present challenges to sustainable growth (Ariyani, Ummah, & Nuraini, 2024). State financial management involves two fundamental aspects: revenue generation and expenditure allocation (Halim, 2016). In this context, the State Revenue and Expenditure Budget (*Anggaran Pendapatan*

dan Belanja Negara, APBN) functions as the government's primary instrument for effective financial management. The ideal fiscal condition occurs when expenditures do not exceed revenues, creating a surplus available for investment. However, as a developing nation, Indonesia continues to rely on debt financing to address budget deficits.

During the pandemic period through 2023, the government implemented an expansionary fiscal policy by increasing state expenditures to stimulate economic growth while maintaining the budget deficit within safe parameters. This policy was designed to support national priority programs as economic stimuli while ensuring fiscal sustainability. To cover the deficit, the government utilized various financing sources, carefully considering efficiency and risk factors.

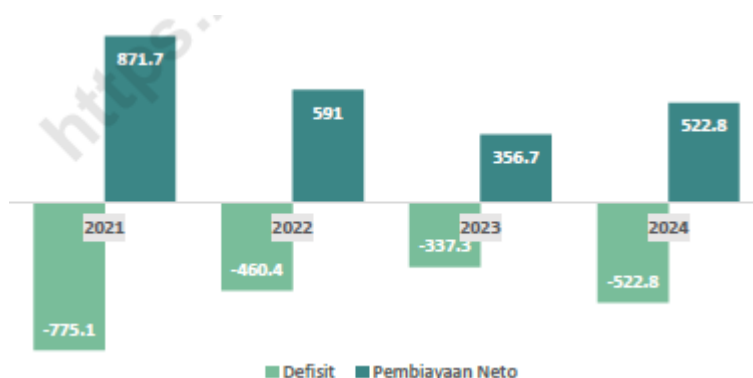


Figure 1. Budget deficit and net financing realization (in trillion rupiah)

Source: Indonesia economic report, 2024

Figure 1 illustrates that the realized deficit and net financing in 2021-2023 successfully covered the budget deficit. However, the 2024 APBN projects a larger deficit of 522.8 trillion IDR, accounting for potential economic risks and financing challenges. Budget deficits, which occur when government expenditures surpass revenues, represent a common fiscal challenge faced by many nations, including Indonesia. The primary source of deficit financing comes from debt, which is managed prudently to maintain market confidence.

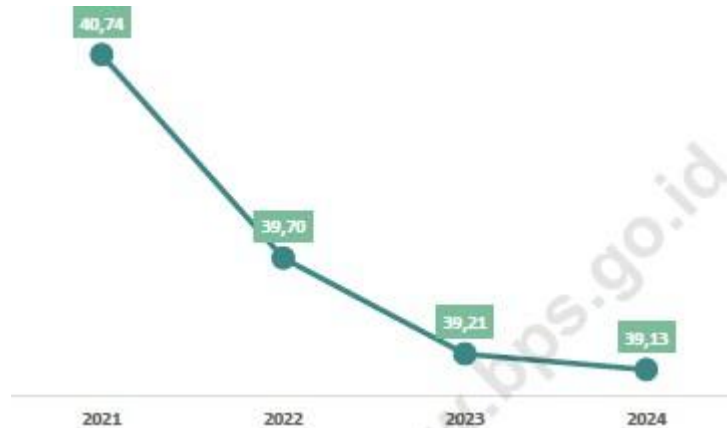


Figure 2. Realized Debt-to-GDP ratio

Source: Indonesia economic report, 2024

Figure 2 demonstrates Indonesia's debt-to-GDP ratio, which has remained stable at 39% over the past three years. This ratio remains within safe limits as it stays below the 60% of GDP threshold. Notably, the 2023 APBN achieved a primary balance surplus of 102.59 trillion IDR, marking a significant milestone after twelve consecutive years of primary balance deficits. This surplus indicates the government's capacity to service debt obligations without requiring additional financing. However, the 2024 APBN faces liquidity challenges stemming from the U.S. Federal Reserve's monetary policy normalization, which may trigger capital outflows and increase yields on Government Securities (*Surat Berharga Negara*, SBN). Additionally, domestic economic recovery may constrain the banking sector's ability to participate in debt financing due to increasing credit demands.

To address these challenges, the government has formulated an innovative and cautious debt financing strategy for 2024. This approach includes issuing medium-to-long-term fixed-rate debt instruments, utilizing idle cash from Public Service Agencies (*Badan Layanan Umum*, BLU) and Budget Surplus Carryovers (*Saldo Anggaran Lebih*, SAL), and developing creative financing mechanisms such as blended financing and Government-Business Entity Cooperation (*Kerjasama Pemerintah dan Badan Usaha*, KPBU). A particularly significant innovation involves the issuance of sukuk (Islamic bonds) and the development of Islamic crowdfunding platforms, which provide alternative financing solutions for small and

medium-scale projects. Crowdfunding enables broader public participation in investment activities while reducing dependence on foreign debt. Research by Nafisha et al. (2024) demonstrates that financial institutions play a crucial role in facilitating Islamic crowdfunding by connecting suitable projects with potential investors. Meanwhile, sukuk has evolved into a sustainable financing instrument, especially for education and healthcare infrastructure projects that generate substantial social impact.

The Indonesian government has pioneered the integration of crowdfunding and sukuk through the launch of sharia Securities Crowdfunding (SCF) based on Sukuk in 2020. This initiative operates under Financial Services Authority (*Otoritas Jasa Keuangan*, OJK) Regulation No. 57/POJK.04/2020 concerning Securities Offerings Through Information Technology-Based Crowdfunding Services, subsequently refined by OJK Regulation No. 16/POJK.04/2021. These regulations expand upon the earlier OJK Regulation No. 37/POJK.04/2018, which initially only covered equity crowdfunding. In 2022, the OJK issued Circular No. 03/SEOJK.04/2022 to provide clearer guidelines for determining sharia-compliant securities in technology-based crowdfunding services. The development of sharia SCF in Indonesia has shown remarkable progress, with 15 registered platform operators as reported by the National Committee for Islamic Economics and Finance (KNEKS) in 2022 (Komite Nasional Ekonomi Keuangan Syariah (KNEKS), 2022).

Syamsuri et al. (2023) found that sharia SCF based on sukuk offers innovative financing solutions compliant with Islamic principles, particularly benefiting halal micro, small, and medium enterprises (MSMEs). These platforms provide more transparent and efficient access to capital while supporting sustainable growth in the Islamic economy. The mandatory electronic halal certification requirement further strengthens Indonesia's position in the global halal market. However, the primary challenge lies in insufficient outreach and education for MSME actors, requiring coordinated efforts among government agencies, financial institutions, and platform operators to maximize the benefits of these innovative financing tools. Concurrently, Arifin and Wisudanto (2017) emphasize the potential of crowdfunding as an alternative infrastructure financing mechanism. Although its current contribution remains modest compared to overall development

needs, the technological proficiency of the millennial generation could significantly drive the expansion of this financing model in coming years. Social capital also plays a pivotal role in determining the success of crowdfunded projects.

Sovereign Sukuk (*Surat Berharga Syariah Negara*, SBSN) has demonstrated its effectiveness as an instrument for financing state budget deficits and government projects. Nisak (2022) explains that SBSN issuance serves not only to cover budget shortfalls but also acts as a catalyst for economic growth and the development of Islamic finance. Through various contract types and sukuk structures, the government has successfully diversified its investor base while providing sharia-compliant investment opportunities for the public. Nevertheless, foreign borrowing remains a financing option, albeit one that requires careful management. Juliani (2021) stresses that external debt must account for repayment capacity to avoid burdening future generations. Foreign loans should complement domestic funding sources, with priority given to projects that accelerate economic development.

This research holds particular significance due to the pressing need for innovative financing solutions that address fiscal deficits while adhering to sustainable development principles. Islamic financial instruments such as sukuk and sharia-compliant crowdfunding schemes offer substantial potential as alternative financing mechanisms and as tools to enhance financial inclusion. The study gains additional relevance from Indonesia's commitment to achieving the Sustainable Development Goals (SDGs) and building a more inclusive economy. The research contributes to academic literature through two primary aspects: first, by developing a theoretical framework that integrates Islamic principles, fiscal policy, and participatory financing models; and second, by formulating evidence-based policy recommendations for optimizing sharia SCF, including strategies for MSME engagement and institutional collaboration. This comprehensive approach makes the study valuable not only for fiscal policymakers but also for the broader development of Islamic economics at the global level.

Literature review

State Revenue and Expenditure Budget (APBN)

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The State Revenue and Expenditure Budget (APBN) is a concrete manifestation of state financial management, established annually through legislation. Structurally, the APBN consists of three main components: revenue, expenditure, and financing. In its formulation, the government employs various macroeconomic indicators as references, including Gross Domestic Product (GDP), economic growth rate, inflation, the exchange rate of the rupiah, the 3-month SBI interest rate, Indonesian oil prices, and national oil production. At its core, the budget is an estimate of revenues and expenditures over a specific period, functioning as a spending plan constrained by revenue capacity, with the aim of maintaining fiscal balance and preventing waste. The budget can serve merely as an instrument for recording state revenues and expenditures, thus acting only as a basic guideline for the inflow and outflow of state finances (Rahayu, 2010).

The concept of state revenue, in a broader perspective, encompasses all government receipts from various sources, including tax revenues, proceeds from the sale of government-owned goods/services, government borrowing, and even the issuance of new currency (Basri & Subri, 2005). In the modern context, the contribution of taxes to national revenue has become highly significant, often serving as the primary source of state income. On the other hand, state expenditure is defined as all central government obligations recognized as deductions from net worth. Optimizing state expenditure is crucial to ensure that fund allocation is effectively and efficiently targeted in line with the government's strategic planning.

State expenditure is broadly divided into two main categories. First, central government expenditure, allocated to finance various development activities at both the national and regional levels. Central expenditure components include personnel spending, goods procurement, capital expenditure, debt interest payments, fuel subsidies, grant expenditures, social spending, and other expenditures. Second, regional expenditure, which consists of fund transfers from the central government to regional governments, subsequently managed through the Regional Revenue and Expenditure Budget (APBD). Regional expenditure includes

revenue-sharing funds, general allocation funds, special allocation funds, and special autonomy funds.

Fundamentally, state expenditure serves to support the execution of central government duties and achieve fiscal balance between the central and regional governments. The optimal use of expenditure budgets is critical in determining the success of economic growth targets. Moreover, state spending patterns inherently reflect government policies and development priorities. Every government decision to purchase specific goods and services is reflected in the composition and magnitude of the expenditure budget, making the APBN a representation of the direction and strategy of national development.

Financing

In the context of state financial management, financing encompasses all government financial transactions, including both receipts and expenditures that must be paid or will be received in the future. Within the framework of government budgeting, financing is intended to cover deficits or utilize budget surpluses. Financing receipts can originate from two primary sources: borrowing and investment returns. Meanwhile, financing expenditures are allocated for three key purposes: repayment of principal debt, provision of loans to other entities, and government capital injections. Broadly, this financing concept is divided into two main categories: domestic financing and foreign financing.

Domestic financing includes all funding sources from individuals or institutions within Indonesia, encompassing various instruments such as banking financing, privatization, government securities, and state capital participation. On the other hand, foreign financing consists of two main components: foreign loan drawdowns (including program loans and project loans) and principal repayments of foreign debt (covering maturities and moratoriums) (Rahayu, 2010). Essentially, debt financing serves as an instrument to cover state budget deficits, yet its role is not limited to this function alone. From a long-term perspective, debt management must also function as a portfolio management tool to support fiscal sustainability.

The concept of fiscal sustainability refers to a condition where the state budget (APBN) structure dynamically fulfills a dual role: as an economic stabilizer while meeting various expenditure

obligations –both explicit and implicit– for present and future needs in a sustainable manner. Fiscal sustainability can be achieved through three main pillars: the ability to control budget deficits, the provision of appropriate fiscal stimulus, and the assurance of timely repayment of all obligations.

APBN financing through foreign debt has been implemented over an extended period with diverse sources. Generally, foreign borrowing sources can be classified into three categories:

1. Bilateral loans from institutions or countries, such as the Japan Bank for International Cooperation (JBIC) under the Japanese government or the Agence Française de Développement (AFD) under the French government;
2. Multilateral loans from institutions like the Asian Development Bank (ADB), World Bank, Islamic Development Bank (IDB), and International Fund for Agricultural Development (IFAD); and
3. Commercial loans, including export credit facilities guaranteed by Export Credit Agencies (ECAs) as well as purely commercial loans.

The majority of government borrowing is allocated to finance activities carried out by ministries/agencies, regional governments, or State-Owned Enterprises (*Badan Usaha Milik Negara*, BUMN). In managing debt, the government adheres to four interrelated key principles:

1. Prudence – emphasizes risk control by maintaining the debt-to-Gross Domestic Product (GDP) ratio within a safe limit of 27.0–29.0%.
2. Minimum Cost of Debt – aims to enhance debt cost efficiency at a controlled risk level while supporting fiscal sustainability.
3. Productivity – ensures that borrowed funds are utilized for productive activities aligned with national development targets.
4. Balance – maintains a controlled debt composition to mitigate risks and preserve macroeconomic stability.

These four principles form a comprehensive debt policy framework, ensuring that debt financing not only meets short-term needs but also supports sustainable long-term development.

Budget deficit

Literally, a deficit refers to a financial shortfall in an organization's treasury, particularly in government, when expenditures exceed revenues. This condition is the opposite of a surplus, which occurs when revenues surpass expenditures. The phenomenon of budget deficits is not new in the history of state finances; in fact, it has been recognized long before the advent of modern budgeting concepts. In the past, various kingdoms and states often resorted to borrowing from merchants or moneylenders to finance urgent needs such as wars, royal ceremonies, or natural disaster responses. In the modern context, budget deficits can arise due to two main factors: first, due to insufficient available funds, and second, because of inappropriate financing methods in budget management.

From an economic perspective, a budget deficit indicates a situation where government consumption exceeds its revenue, necessitating the shortfall to be covered by drawing from individual or societal income. This creates an imbalance where total demand for goods and services exceeds total available supply, particularly in a closed economic system that restricts foreign trade. A budget is a detailed list or statement of expected state revenues and expenditures over a specific period, usually one year (Basri & Subri, 2005). A budget deficit is deliberately planned when the government seeks to stimulate economic growth, especially during a recession, where government spending (G) is intentionally set higher than revenue (T) to boost economic activity.

From a fiscal policy perspective, deficit budgets often serve as a crucial tool for governments to stimulate the economy. When the private sector contracts during a recession, increased government spending through budget deficits can generate the necessary aggregate demand to sustain production levels and employment. However, this policy also carries risks if not managed properly, particularly concerning the accumulation of government debt and inflationary pressures that may arise from increased aggregate demand unaccompanied by expanded production capacity. Therefore, a comprehensive understanding of budget deficit mechanisms and their implications is essential for policymakers in designing sustainable and effective financing strategies to promote economic growth.

Budget deficits are an economic phenomenon influenced by various complex factors. According to Brixi and Mody (2002), several key variables significantly affect a country's budget deficit conditions:

1. Economic growth

Economic growth plays a central role in determining a nation's fiscal health. When Gross Domestic Product (GDP) increases, it stimulates activity in the real sector and businesses, thereby boosting government revenue through taxation. Enhanced economic activity leads to higher corporate profits, increasing income from taxes such as income tax, value-added tax, and excise duties. Tax revenue, as the primary component of domestic revenue, is expected to turn a budget deficit into a surplus or at least reduce its magnitude in subsequent periods.

2. Exchange rates

Exchange rates also significantly impact budget deficits, particularly for countries like Indonesia that rely on foreign loans. Kuncoro (2011) explains that fluctuations in the rupiah's value against foreign currencies, especially the US dollar, can strain the state budget. When the rupiah depreciates, the rupiah-denominated principal and interest payments on foreign loans increase, thereby raising budgetary burdens and widening the deficit. This phenomenon highlights the vulnerability of national financial systems to foreign exchange volatility.

3. Global oil prices

Global oil prices are another external factor influencing budget deficits. Surjadi (2006) argues that rising oil prices can alter a country's trade balance and exchange rate. For net oil-importing countries like Indonesia, higher oil prices worsen the balance of payments and pressure the exchange rate. The ripple effects include increased import costs and reduced export values, ultimately diminishing real national income. This situation is often accompanied by high inflation, unemployment, and sluggish economic growth—all factors contributing to larger budget deficits.

4. Inflation

Inflation, as a persistent rise in general price levels, indirectly affects budget deficits. Higher prices for goods and services reduce public purchasing power, leading to decreased demand and

production. Lower real output suppresses real GDP and economic growth, thereby reducing state revenue. Meanwhile, the government must still meet public needs, making budget deficits more likely to expand under high inflation.

5. Interest rates

Interest rates influence budget deficits through a more direct mechanism, particularly in debt financing via the issuance of Government Securities (SBN). Rising interest rates increase the burden of interest and principal payments on SBN, including Government Bonds (*Surat Utang Negara*, SUN) and Sharia Government Securities (SBSN). These escalating payments directly add to budgetary burdens and can widen the deficit (Putra et al., 2025).

State budget formulation requires careful consideration of expenditure priorities based on government strategic plans. Deficit budgeting is often used as an economic stimulus tool, but its implementation in the State Revenue and Expenditure Budget (APBN) must balance development needs with fiscal capacity. In recent years, Indonesia has adopted an expansive fiscal policy through deficit budgets to support national development priority programs. However, as demonstrated by the 1958-1968 experience (Sudirman, 2011), this policy carries inflation risks if mismanaged. During that period, budget deficits financed through foreign loans eventually triggered high inflation, undermining economic stability.

To minimize the negative impacts of budget deficits, the government implements various control measures. Limiting the APBN deficit to a maximum of 3% of GDP is one principle of sound fiscal management. Other strategies include refocusing priority programs on infrastructure development, improving education and healthcare quality, and social protection. On the revenue side, tax reforms –such as data integration, enhanced taxpayer compliance, broadening the tax base, and combating tax avoidance– serve as strategic efforts to strengthen state revenue. This multidimensional approach is expected to keep budget deficits at manageable levels while promoting sustainable economic growth.

Research methods

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This study employs a descriptive qualitative method with a literature study (library research) approach. The research aims to analyze alternative deficit financing through Islamic financial instruments, specifically sukuk, Islamic crowdfunding, and sukuk-based securities crowdfunding. The qualitative method was chosen as it aligns with the exploratory and interpretative nature of the research, enabling the researcher to gain an in-depth understanding of the phenomenon through non-numerical data analysis. The literature study approach allows the researcher to collect and analyze various written sources relevant to the research topic.

The data sources used in this study consist of secondary data obtained from official government documents, academic literature, and historical records. Official documents include reports from the Ministry of Finance, the Central Statistics Agency (*Badan Pusat Statistik*, BPS), the Financial Services Authority (OJK), and the National Committee for Sharia Economics and Finance (KNEKS). Academic literature encompasses reputable journals, textbooks, and relevant regulations, such as Law No. 19 of 2008 on Sovereign Sharia Securities (SBSN) and OJK Regulation No. 57/POJK.04/2020. Historical data includes the realization of the state budget (APBN), budget deficits, and debt-to-GDP ratios from 2018–2024.

The data collection technique applied was documentation, in which the researcher gathered and selected secondary data based on credibility, relevance, and timeliness criteria. Data sources were chosen from official institutions or indexed publications to ensure credibility. The data must also be relevant to Islamic finance, fiscal policy, and state budget deficit topics.

Data analysis was conducted inductively through three main stages. First, theme identification was carried out by categorizing findings based on deficit causes, sharia instruments, and supporting regulations. Second, source triangulation was performed by comparing findings from literature, policy documents, and official reports to validate data consistency. Third, critical interpretation was conducted by linking the analysis results to sharia economic theories, such as the principle of *maslahah* (public benefit) and the prohibition of *riba* (usury), as well as conventional fiscal policy frameworks.

Results and discussion

Sharia-compliant deficit financing in budgeting

In Islamic teachings, humans are granted considerable freedom to fulfill their livelihood needs as long as they do not contravene the provisions of the Qur'an and Sunnah. One of the strict prohibitions in Islamic economics is the practice of *riba* (usury), which can be definitively understood as the taking of excess in various economic transactions that violate sharia principles and rulings. This prohibition is absolute, as emphasized in Allah's decree in surah Al-Baqarah/:278), "*O you who have believed, fear Allah and give up what remains [due to you] of interest if you should be believers.*" This verse not only explicitly prohibits *riba* but also highlights that such practices inherently involve injustice (*zulm*) toward one of the transacting parties. In the modern context, this prohibition extends to interest-based lending or debt transactions, classified in *fiqh* terminology as *ribā al-nasī'ah* (usury arising from delay).

In state financial management, deficit budgeting is a fiscal instrument frequently employed by governments. The conventional mechanism for covering deficits typically involves debt financing, which often incorporates interest elements. An examination of Indonesia's 2018 Draft State Budget (*Rancangan Anggaran Pendapatan dan Belanja Negara*, RAPBN) reveals two primary classifications of government debt financing: first, through the issuance of Government Securities (SBN), and second, through direct borrowing. SBNs are debt acknowledgment instruments issued in either domestic or foreign currency, wherein the state guarantees the payment of principal and interest according to their maturity periods. In practice, the dominant instruments used are Government Bonds (SUN) and Sovereign Islamic Securities (*Surat Berharga Syariah Negara*, SBSN). Meanwhile, loan components originate from two sources: domestic and foreign borrowing.

From an Islamic perspective, budget formulation emphasizes the importance of effectiveness and efficiency in state financial management. This approach ensures that budget allocations are precisely targeted, thereby minimizing the occurrence of deficits. Logically, if deficits can be avoided, the need for borrowing would also decrease. However, in reality, when borrowing becomes necessary, the government must allocate specific funds to pay

interest on such loans. From the lens of *fiqh al-muamalah* (Islamic commercial jurisprudence), this interest constitutes an excess (*ziyādah*) in loan transactions, which is unequivocally categorized as *ribawi* (usurious). The core issue lies in the nature of interest as an obligatory additional value in loan agreements, which sharia considers a form of economic exploitation (*zulm*).

Islamic economics fundamentally differs from conventional economics in its perception of money. In the Islamic paradigm, money is regarded solely as a medium of exchange that must continuously circulate within society (*flow concept*), whereas capital is treated as a *stock concept*. The logical consequence of this view is that money cannot generate income unless it is invested in the real sector. In other words, money can function as productive capital only when allocated or invested in real economic activities, thereby yielding income that is sharia-compliant. This contrasts sharply with the conventional concept of the *time value of money*, which permits profit generation without real-sector investment. This fundamental distinction forms the theological basis for the prohibition of interest in Islam.

The foundational principles of Islamic economics actually allow broad freedom in economic activities, as reflected in the principle of *hurriyyah* (freedom), which serves as a pillar of the Islamic economic system. In this context, the government has the authority to adopt various economic policies as long as they do not transgress sharia-defined prohibitions. Deficit budgeting, in principle, is not inherently contradictory to Islamic teachings unless it incorporates prohibited elements. However, the problem arises when deficit financing relies on interest-based borrowing mechanisms, which clearly violate sharia principles.

The principle of *tawhīd* (divine unity), as the cornerstone of Islamic economics, demands that all economic activities align with sharia values. As God's vicegerents (*khalīfah*) on earth, humans are obligated to act in accordance with Allah's decrees and bear full responsibility for their actions. In the context of state financial management, the use of interest-based systems for deficit financing constitutes a violation of this principle. Such usurious practices also contradict the Islamic principle of justice (*ʿadl*), which ensures that no party is wronged in any transaction. The mechanism of loan

interest, whether direct or indirect, inherently creates injustice, as it systematically disadvantages one party.

From an Islamic economic perspective, the government bears the trust (*amānah*) of *khilāfah* (stewardship) and is tasked with implementing sharia on earth. As the manager of public affairs, the government holds a significant responsibility to ensure the economy operates in accordance with Islamic principles. Its regulatory functions must be exercised with full awareness of accountability before Allah. Economic policies must prioritize public welfare (*maṣlahah*) and ensure equitable income distribution. In this regard, deficit budgeting reliant on interest-based financing violates the core tenets of Islamic economics. As the representative of *khilāfah*, the government must refrain from policies involving *riba*, which is explicitly prohibited in Islam.

Based on the above comprehensive analysis, it can be concluded that deficit budgeting mechanisms incorporating interest-based financing are incompatible with Islamic economic principles. From the perspective of *tawhīd*, the imposition of interest contradicts the concept of *ilāhiyyah* (divine authority). From the standpoint of justice, interest mechanisms perpetuate systemic inequity. And from the angle of governmental responsibility, such policies reflect the state's failure to uphold its duty as *khalīfah* in consistently applying Islamic law.

Islamic economics offers alternative solutions that align with sharia principles. First, the government can optimize balanced budgeting policies, wherein expenditures are adjusted to revenue capacity, while maintaining fiscal efficiency and effectiveness. This approach must be supported by anti-corruption measures and state revenue optimization to sustain economic growth. Second, if deficit policies are unavoidable, the government should prioritize sharia-compliant instruments such as Sovereign Islamic Securities (SBSN) and avoid interest-based foreign borrowing. Thus, economic development can proceed without compromising the foundational principles of Islamic sharia.

Financing budget deficit solutions with Islamic financial instruments

Sukuk

The Indonesian government has developed Islamic financial instruments since 2004 as a sharia-compliant solution for financing budget deficits. An in-depth study of these instruments aims to meet the needs of investors who require sharia compliance in every transaction. Islamic economics, founded on principles of morality and justice, is derived from three primary sources: the Qur'an, Hadith, and Ijma' (scholarly consensus). Every Islamic transaction must fulfill the criteria of fairness (*'adl*), permissibility (*ḥalāl*), goodness (*ṭayyib*), and social benefit (*maṣlaḥat*), while avoiding all forms of MAGHRIB (*maysīr* [gambling], *gharār* [excessive uncertainty], *riba* [usury], and *bāṭil* [invalid transactions]). A fundamental principle in Islamic transactions is the necessity of an underlying asset, whether in the form of fixed assets or specific projects, as the basis for financing.

The legal framework for issuing Islamic financial instruments in Indonesia is specifically regulated under Law No. 19 of 2008 on Sovereign Sharia Securities (SBSN). This regulation provides a legal foundation for the government to manage sharia-compliant portfolios, utilize state-owned assets as underlying assets, and establish issuing companies that function as trustees.

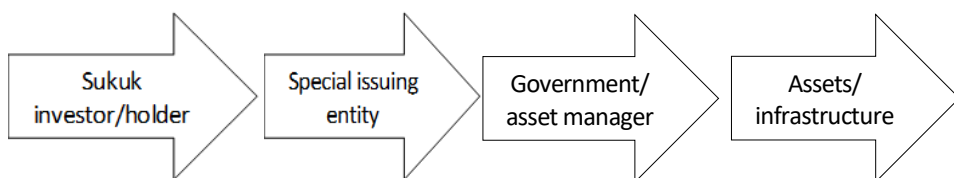
Various types of sharia contracts (*akad*) can be applied in sukuk issuance, including *ijārah* (leasing), *muḍārabah* (profit-sharing), *mushārah* (joint venture), *murābahah* (cost-plus sale), *wakālah* (agency), and *istiṣnā'* (project financing). However, in practice, three types of sukuk are most commonly used: (1) retail sukuk (SR) with an *ijārah* contract, (2) Savings sukuk (ST) with an *ijārah* contract, and retail waqf sukuk (SWR) with a wakalah contract. Table 1 analyzes the differences between these three primary sukuk types.

Table 1. Comparison of Retail Sukuk (SR), Savings Sukuk (ST), and Retail Waqf Sukuk (SWR)

| No | Feature | Retail Sukuk (SR) | Savings Sukuk (ST) | Retail Waqf Sukuk (SWR) |
|----|----------------------|------------------------|------------------------|-------------------------|
| 1 | Purpose | State budget financing | State budget financing | Productive waqf |
| 2 | Return | Fixed | Floating | Fixed |
| 3 | Liquidity | Tradable | Non-tradable | Non-tradable |
| 4 | Principal Redemption | Yes | Yes | Yes |
| 5 | Profit Distribution | Monthly | Monthly | None |

Conceptually, sukuk are defined as securities representing ownership claims (beneficial rights) over assets, whether tangible, intangible, or specific projects. The sukuk issuer is obligated to: (1) distribute profit-sharing income to sukuk holders, (2) return the principal amount upon maturity, and (3) ensure the entire transaction process complies with sharia principles.

The sukuk issuance mechanism can be illustrated through Figure 3:

**Figure 3.** Sukuk issuance mechanism

Sukuk can be issued by various entities. First, government: through Retail Sukuk (SR) and global sukuk issued by the Ministry of Finance via Indonesia SBSN Issuing Company III (PPSI-III) to finance infrastructure projects. Second, corporations/financial institutions; for business expansion or other investment purposes.

In international practice, sukuk issuances typically employ three primary methods (Syaripudin, Sulthonuddin, Furkony, & Abdul Hamid, 2022). The bookbuilding method operates through a securities issuance mechanism where investors submit purchase bids specifying both quantity and price (yield), with all bids recorded in an order book maintained by an investment bank acting as bookrunner, enabling optimal price discovery based on market demand. Alternatively, the auction method utilizes a competitive bidding system where participants may submit either competitive bids (with specified price/yield parameters) or non-competitive bids (without price specifications), with the entire process conducted

within a predetermined timeframe through a dedicated electronic platform managed by the auction agent. Finally, private placement involves restricted issuance to predetermined investors through bilaterally negotiated terms, where sukuk are typically issued via a Special Purpose Vehicle (SPV) as the issuing entity, though certain exceptions permit direct issuance by the originator or obligor without SPV involvement.

Crowdfunding

Crowdfunding has emerged as an innovative fundraising method that utilizes online platforms to connect various projects with potential investors. In Indonesia, the development of crowdfunding in recent years has shown significant progress, offering an attractive financing alternative for both the government and businesses. Data from the Financial Services Authority (OJK) recorded crowdfunding transactions in Indonesia reaching IDR 1 trillion in 2022, a figure that demonstrates its substantial potential in supporting sustainable development projects. Crowdfunding regulations in Indonesia are governed by the Financial Services Authority Regulation No. 77/POJK.01/2016 on Information Technology-Based Lending Services, which ensures transaction security by requiring crowdfunding platform operators to be legally established as limited liability companies or cooperatives.

The success of crowdfunding in Indonesia can be observed in various tangible projects, one of which is the development of eco-friendly infrastructure successfully funded through crowdfunding platforms. Such projects not only help address budget deficits but also play a role in raising public awareness of the importance of sustainable development. According to Dwiastuti (2020), projects involving public participation in funding tend to be more successful and sustainable as they foster a sense of ownership among the community. Nevertheless, the development of crowdfunding in Indonesia still faces several challenges, particularly related to the regulatory framework that is not yet fully supportive. As highlighted by Nurwahida et al. (2022), close collaboration between the government and various stakeholders is necessary to establish clearer regulations that support the growth of crowdfunding as an alternative financing source.

Another critical challenge is the relatively low level of public understanding regarding crowdfunding mechanisms. Many people still do not fully grasp the concept of crowdfunding or how to

participate in the projects offered. Therefore, intensive educational efforts and clear, transparent dissemination of information are essential to increase public interest in investing through crowdfunding platforms. With appropriate support from the government and other stakeholders, crowdfunding has significant potential to become a sustainable financing strategy for addressing budget deficits while funding projects that deliver tangible benefits to society and the environment.

In the Islamic context, crowdfunding has evolved into an appealing instrument based on principles compliant with Islamic law. Sharia-compliant crowdfunding refers to the online fundraising from the public conducted in accordance with Islamic principles, free from usury (*riba*) and aligned with sharia-compliant objectives. The collected funds can be allocated for various purposes, such as financing MSMEs (Micro, Small, and Medium Enterprises), social projects (waqf, zakat, infaq), halal startups, or sharia-compliant property financing. Several sharia-compliant crowdfunding schemes exist, including: (1) equity-based crowdfunding (using *muḍārabah* or *mushārah* contracts), (2) donation-based crowdfunding (for social or charitable purposes), (3) reward-based crowdfunding (for halal creative projects where donors receive gifts), and (4) lending-based crowdfunding (using *qard al-hasan* loans, where only the principal is repaid). The basic mechanism of crowdfunding is illustrated in Figure 4.

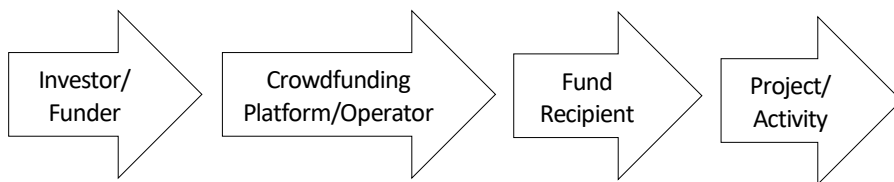


Figure 4. Crowdfunding mechanism

A recent development in sharia-compliant crowdfunding is the emergence of sukuk-based Islamic securities crowdfunding, which combines crowdfunding principles with well-established Islamic financial instruments. This innovation opens new opportunities for financing sharia-compliant projects while providing investment alternatives that adhere to Islamic principles. With its various advantages and potential, sukuk-based Islamic crowdfunding is expected to become a key pillar in Indonesia's Islamic financial system.

Sharia-based sukuk securities crowdfunding

Sharia-based sukuk Securities Crowdfunding (SCF) has brought a transformative impact on the development of halal Micro and Small Enterprises (MSEs) in Indonesia. This instrument provides a solution to the limited access to capital that MSEs have long faced in obtaining funding from conventional financial institutions. Through the sharia-compliant SCF mechanism, MSE actors can now access capital from diverse investors via a simpler process that fully adheres to Islamic principles, avoiding interest-based burdens and stringent collateral requirements. More than just a financing alternative, sharia-based SCF also expands financial inclusion by enabling broader public participation –including retail investors with limited capital– to invest in halal MSE projects while earning returns aligned with sharia values.

Within the MSME financing landscape, sharia-based SCF competes with various other instruments, such as the sharia People's Business Credit (*Kredit Usaha Rakyat*, KUR Syariah) program, Islamic banks, Sharia Rural Banks (*Bank Pembiayaan Rakyat Syariah*, BPRS), and sharia Peer-to-Peer (P2P) financing. To enhance competitiveness, sharia-based SCF providers can adopt two key strategies: First, a cost leadership strategy through operational cost efficiency to increase public interest and awareness. Second, a differentiation strategy by offering a unique value proposition that makes sharia-based SCF a more attractive investment and financing option compared to alternatives.

The primary characteristic of sharia-based SCF is the simplified sukuk/equity issuance process compared to conventional securities issuance mechanisms on the Indonesia Stock Exchange (IDX). However, sharia-based SCF providers bear complex multi-roles, as outlined by the National Committee for Sharia Economics and Finance (Komite Nasional Ekonomi Keuangan Syariah (KNEKS), 2022), including: (1) functioning as a mini exchange, (2) conducting pre-screening of potential issuers, (3) applying sharia screening, (4) acting as a trustee, and (5) establishing and managing the sharia-compliant securities list. The sharia foundation of sukuk-based SCF has been legitimized through Fatwa DSN MUI No. 140/DSN-MUI/VIII, which governs this *muamalah* activity, emphasizing principles of honesty, trustworthiness, and issuer accountability.

The key advantage of sukuk-based sharia SCF lies in its ability to bridge the financing needs of halal MSEs with the investment

preferences of Muslim communities. This mechanism connects MSEs as issuers with investors through digital platforms, offering easy access to collateral-free financing and periodic profit-sharing dividends –distinct from conventional banking mechanisms. Figure 5 illustrates the operational mechanism of sukuk-based sharia SCF:

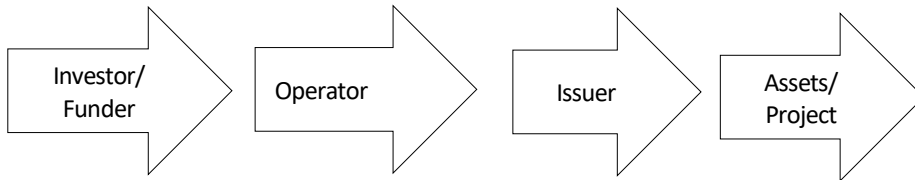


Figure 5. Sukuk-based sharia SCF mechanism

The sharia-based SCF ecosystem involves four main stakeholders, each with distinct roles:

1. Financial Services Authority (OJK): Acts as the regulator, granting operational licenses, supervising, and monitoring platform activities.
2. Platform Operators: Serve as facilitators, organizing sukuk offerings while conducting issuer and investor screening.
3. Issuers: Legal entities with a maximum asset value of IDR 10 billion, utilizing the platform to secure funding.
4. Investors: After fulfilling requirements (e.g., having a securities account with a custodian bank), they can participate in sukuk purchases via the platform.

In Indonesia, several OJK-licensed SCF operators include Bizhare, Crowddana, Danasaham, Fundex, ICX, LBS, Santara, Shafiq, Ekuid, Danamart, Fulusme, Visiku, Vestora, Urun RI, and Aindo.

The emergence of sukuk-based sharia SCF not only addresses the classic financing challenges of halal MSEs but also fosters an inclusive, sharia-compliant investment ecosystem. This instrument serves as tangible evidence of how Islamic financial innovation can tackle MSME financing challenges while promoting equitable and sustainable economic growth.

Conclusion

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This study examines alternative deficit financing mechanisms through Islamic financial instruments, focusing on sukuk, Islamic crowdfunding, and sukuk-based securities crowdfunding. The findings demonstrate that these instruments not only effectively address budget deficits but also align with sharia principles such as justice (*'adl*), public benefit (*maṣlaḥah*), and social responsibility (*ukhuwwah ijtīmā'iyah*). Islamic financing has been proven to enhance public participation in development, expand financial inclusion, and reduce reliance on interest-bearing debt, thereby fostering a more sustainable financial system.

Furthermore, this research identifies that sukuk-based Islamic securities crowdfunding holds significant potential in supporting financing for halal micro, small, and medium enterprises (MSMEs) and infrastructure projects. This instrument facilitates more inclusive access to capital for businesses while providing sharia-compliant investment alternatives for the public. These findings reinforce the argument that Islamic financing serves not only as a fiscal solution but also as a catalyst for value-based economic growth grounded in Islamic principles.

Nevertheless, this study has several limitations, including reliance on secondary data and the absence of quantitative analysis to empirically measure economic impact. Future research should conduct field studies to evaluate the effectiveness of implementing Islamic crowdfunding and sukuk in deficit financing contexts. Additionally, more structured policy models should be developed to strengthen the regulatory framework and enhance public and business awareness of Islamic financial instruments.

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