Published by Lembaga Penerbitan, Penelitian, dan Pengabdian kepada Masyarakat
Universitas Nurul Jadid Paiton Probolinggo, Indonesia.
online access at https://ejournal.unuja.ac.id/index.php/hakam
e-ISSN 2580-8052 | p-ISSN 2829-5803

hakam
Jurnal Kajian Hukum Islam dan Hukum Ekonomi Islam

Volume 10 Number 2 (June 2026) | Pages 658 – 673
Doi: https://doi.org/10.33650/jhi.v10i2.14955
Submitted: April 12, 2026 | Revised: June 7, 2026 | Accepted: June 7, 2026| Published: June 15, 2026

THE BUREAUCRATIZATION OF FAITH: THE POLITICAL BACKDROP OF INDONESIA'S FIRST SHARIA-COMPLIANT ECONOMIC LEGISLATION

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ABSTRACT

This study examines the political backdrop of the rise of Sharia-compliant economic rules during the final decade of Indonesia's New Order regime. Through a critical lens of political economy, this study aims at analyzing the political-historical landscape that facilitated the birth of the nation's first Islamic banking. Using a qualitative approach, this study employs a historical perspective to investigate the convergence of state power and legislative policy during the late 1980s and early 1990s. The research results indicate that the enactment of the Law No 7 of 1992 on Banking, which becomes the foundation of Islamic finance, served primarily as a strategic tool of state diplomacy aimed at perpetuating the New Order's hegemony. Drawing on Tarek Masoud's political economy framework, this study argues that Suharto pivoted toward a Sharia-compliant economic system to secure a new foundation of legitimacy among the burgeoning educated Muslim middle class. This maneuver was a calculated response to mitigate declining support from secular military factions and to co-opt the moral reputational advantage of Islamic institutions.

Keywords : *Islamic Banking; New Order; Political Economy; Islamic Economic Law*

ABSTRAK

Studi ini meneliti latar belakang politik lahirnya peraturan ekonomi syariah selama dekade terakhir rezim Orde Baru Indonesia. Melalui perspektif ekonomi politik kritis, studi ini bertujuan untuk menganalisis lanskap sejarah-politik yang memfasilitasi lahirnya peraturan perbankan Islam pertama di Indonesia. Dengan pendekatan kualitatif, studi ini menggunakan perspektif historis untuk menyelidiki konvergensi kekuasaan negara dan kebijakan legislatif selama akhir tahun 1980-an dan awal 1990-an. Hasil penelitian menunjukkan bahwa penetapan Undang-Undang Nomor 7 Tahun 1992 tentang Perbankan, yang menjadi dasar keuangan Islam, berfungsi sebagai alat strategis diplomasi negara yang bertujuan untuk melanggengkan hegemoni Orde Baru. Dengan mengacu pada kerangka ekonomi politik Tarek Masoud, studi ini berpendapat bahwa Suharto beralih ke sistem ekonomi syariah untuk mengamankan fondasi legitimasi baru di kalangan kelas menengah Muslim terdidik yang sedang berkembang saat itu. Manuver ini merupakan respons yang diperhitungkan dengan cermat mengingat menurunnya dukungan dari faksi militer sekuler di samping juga untuk memanfaatkan keunggulan reputasi moral lembaga-lembaga keislaman.

Kata Kunci: *Bank Syariah; Orde Baru; Ekonomi Politik; Hukum Ekonomi Islam*

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INTRODUCTION

Being the world's most populous Muslim country (Statistik, 2021), Indonesia is neither a religion-based state nor a secular state. The state's ideology is the *Pancasila*, which is derived from two Sanskrit words, *panca* and *sila*, meaning "five" and "principle" respectively. The five principles of Pancasila are: 1) the belief in one God, 2) a just and civilized humanity, 3) the unity of Indonesia, 4) representative democracy, and 5) social justice for all Indonesians (Hooker, 2008).

The Pancasila is regarded as a middle way between two state concepts. Although religion does not become the state ideology, the state regulates religious affairs through the Ministry of Religious Affairs (MoRA) (Ichwan, 2006) and other governmental bodies, such as the National Board of Zakat Administration (Badan Amil Zakat Nasional/BAZNAS), and Indonesian *Waqf* Board (Badan Wakaf Indonesia/BWI). However, due to this close but ambiguous relationship between religion and the state, there have always been demands to institutionalize Islamic teachings in all aspects of Indonesian Muslims' lives. There are at least two channels for coping with the demands legally: through the incorporation of Islamic law into the Indonesian legal system and through the legislation of Islamic bylaws (*Perda Syariah*) in local governments (Salim, 2008).

The incorporation of Islamic economic law into the Indonesian legal system is one of many attempts at institutionalizing Islamic teachings at a state level. Nevertheless, despite its growing significance, the scholarly literature concerning Islamic economic law remains less extensive than the well-established body of research dedicated to Islamic family law. The focus on the later area is justified by the fact that family law remains the most widely applied aspect of the Sharia in Indonesia and across other Islamic jurisdictions. This phenomenon resulted from the extensive secularization of the Sharia during the colonial period, a process that effectively marginalized Islamic legal influence and left only the domain of *al-aḥwāl al-shakhsiyya* (personal status law) (Hallaq, 2009a).

At the same time, Muslims are only loosely attached to Islamic economic law because there are countless choices of transactions (*muʿāmala*) that are permissible according to Islamic norms. It is stated in the *fiqh* legal maxim, *"al-ashl fi al-mu'āmala al-ibāha hatta yadulla al-dalīl 'alā al-tahrīm",* which means that the default rule for every transaction is permissible unless there is evidence that forbids it (al-Suyuti, 2004). Therefore, the implementation of Islamic economic law is not as dynamic as those in Islamic family law. Nevertheless, there has been an increased awareness of Islamic economic practices, triggered by the rapid growth

of various types of transactions which may contain usury or gambling elements which are prohibited in Islam.

To accommodate the requirement of facilitating usury-free transactions, modern Islamic finance institutions has steadily grown in many Muslim countries since the 1970s. These institutions were named Islamic banks rather than Sharia banks. These are, for instance, the Dubai Islamic Bank (established in 1975), the Faisal Islamic Bank of Egypt (established in 1977), the Islamic Bank of Sudan (established in 1977), and the Jordan Islamic Bank for Finance and Investment (established in 1978) (Warde, 2010).

In the Indonesian context, the terms Sharia and Islamic law are often used interchangeably. In financial sectors, Sharia is most frequently used rather than Islamic law. Attaching the word Sharia on financial institutions or a transaction is meant to convey that it is managed based on Islamic law. This terminological convention is particularly evident in the Indonesian market, which exhibits a broad spectrum of sectors designated as Sharia-compliant, for instance "Sharia banks," "Sharia insurance," "Sharia securities," "Sharia pawning," and even "Sharia hotels."

However, the terms Sharia and Islamic law are scholarly distinguished. Wael B. Hallaq argues that Islamic legal system which is implemented by Muslims today is not the Sharia. (p. 152) It is a narrowed version of Sharia which was created by modernist legal scholars. Islamic law is now thought to be applicable only on personal status (*al-ahwāl al-shakhsīyya*) and is withdrawn from its broader social concerns. The Sharia in pre-modern Muslim societies was not only a judicial system and a legal doctrine but also a discursive practice in which complex relations of social, economic, cultural and moral aspects intersected each other in numerous ways (Hallaq, 2009a). Therefore, Lindsey suggests that in Indonesian context, the use of the term Islamic law is more appropriate since what is implemented is part of a codification process in post-colonial countries (Lindsey, 2012).

As for the formalization of Islamic law in Indonesia, scholars have examined the role of the state in codifying religious ethics. Hosen and Salim examine the shift of Islamic law toward positive law (Hosen, 2007; Salim, 2008), whereas Lindsey highlights the administrative challenges of integrating these elements into the national legal framework (Lindsey, 2012). In addition, Cammack and Feener contend that this process of formalization functions as a mechanism for modern state-building and social transformation, replacing traditional legal diversity with state-controlled frameworks (Cammack, 1997; Feener, 2007).

Meanwhile, another camp of scholars adhering to the instrumentalist perspective suggests that Islamic economic law often serves as a medium for the achieving broader political and societal goals. Hadiz asserts that these legal frameworks facilitate the burgeoning Islamic middle class in exerting political influence (Hadiz, 2011), while Sakai demonstrates how governments utilize Sharia-based finance as an effective strategy for national economic development (Sakai, 2010).

Although the "top-down" structure of Sharia administration in Indonesia is well-documented in the literature, there is insufficient theoretical investigation that examines the political economy of the Islamic economic sector. Contemporary critiques of state-led Islamization have primarily concentrated on domains such as criminal law/*jināyāt* (Feener, 2013), family law/*munākahāt* (Cammack, 1997), and regional Sharia regulations/Perda Sharia (Bush, 2008). This has resulted in insufficient scrutiny of the economic aspect. This study highlights a lack of acknowledgment of Islamic economic law as an advanced instrument for state-led political unification and elite negotiation. This study departs from normative legal critiques, utilizing Tarek Masoud's political economy framework to elucidate the strategic motivations underlying the state-mandated implementation of Sharia banking regulations. This perspective emphasizes how the New Order regime exploited the economic sector to navigate political rivalry, assimilate the Muslim middle class, and establish a new foundation of legitimacy as conventional military backing diminished (Masoud, 2013).

Therefore, the primary objective of this research is to analyze the political-historical landscape of Islamic economic law in Indonesia through a critical democratic lens. How did the political economic changes of the New Order regime in the late 1980s and early 1990s lead to the implementation of the first Islamic finance system in Indonesia? Rather than simply a reaction to a grassroots religious awakening, to what extent was the institutionalization of Islamic banking used as a strategic instrument for elite co-optation and regime stabilization? This paper argues that the implementation of Islamic economic laws in Indonesia primarily served as a tool of state diplomacy aimed at perpetuating the New Order regime's power. Using Tarek Masoud's political economy framework, this study hypothesizes that Suharto turned to a Sharia-compliant financial system to build a new foundation of legitimacy among the growing educated Muslim middle class and to mitigate the declining support of the military. The implementation of the law was a strategic effort to co-opt the Muslim intellectual elite and incorporate the moral reputational superiority of Islamic finance into the state's regulatory framework.

RESEARCH METHOD

This research utilizes a normative legal method with a qualitative framework, employing a historical perspective to analyze the convergence of power and policy. To examine the influence of political dynamics on Islamic economic law in Indonesia, the study employs a historical approach to delineate the chronological development of legal norms, alongside a political-legal framework to assess the effect of state power and ideology on the formalization of these laws. Data were collected through library research, entailing the systematic documentation of primary legal materials, such as national regulations, and secondary sources, including academic literature and socio-political records that elucidate Indonesia's legislative history.

Data analysis employed qualitative-interpretive framework, starting with a heuristic phase to validate sources, succeeded by in-depth textual studies to ensure data validity. The study employs content analysis and deductive reasoning to connect significant political transformations with specific legal changes. Through the integration of historical, political, and normative perspectives, this research uncovers the transformation of Islamic economic principles from religious discourse into positive law. This method shows that the way the law changes is closely linked to the social and political climate.

FINDINGS AND DISCUSSION

Proposing Islamic Law in Secular Indonesia

In political studies, secularism is commonly understood as separating the institution of state from the institution of religion. It came from an assumption that religion is irrational and intolerant and thus in contradiction to the spirit of modernity which gave birth to the nation states. Religion is also regarded as a threat to humanity in the sense that it tends to create war and hostility. Therefore, secular theorists insist that it should be removed or at least privatized. Responding to this view, scholars of Postcolonial studies argue that secularism is not the solution but is the problem. The current development of how religion is believed, understood and publicly practiced show the failure of secularism (Asad, 2003).

The ideas and practices of secularism disseminated during the colonial era through the establishment of modern states, particularly in most Muslim countries (Asad, 2003; Hallaq, 2009b). The secular system left many problems not only for these countries, but also for the Western countries from which it originated. The most noteworthy issues to arise in

the former case is the restriction of Muslims in expressing their ideal norms of Sharia in their own country (Hallaq, 2013). This restriction imposed by the secular state created tension among the citizens of Muslim countries in particular (e.g. in Senegal and Sudan) (Salomon, 2018; Villalon, 1995).

In Indonesia, the interpretation of the ideology of the state, whether or not it is based on the Sharia, has been hotly disputed since the preparation leading up to Indonesia's independence (Boland, 1982). The implementation of the *Pancasila* as the foundation of the state, instead of the *sharīʿa*, gave rise to opposition from a number of Islamic groups that later became rebel movements against the so-called "Unitary State of the Republic of Indonesia" (Aspinall, 2009; van Dijk, 1981).

Although the *Pancasila* is a middle way between religious and secular concepts of the state, many Muslims feel unsatisfied with this compromise. Their dissatisfaction has been expressed in many ways. In post-authoritarian Indonesia, after the opening of democracy, many Islamist groups have been formed (Hilmy, 2010). Some groups have pursued their aspirations politically outside the framework of the government, such as Warriors of Jihad (*Laskar Jihad*), Majelis Mujahidin Indonesia (MMI), Hizbut Tahrir Indonesia (HTI), Jama'ah Tablig, and Islamic Defense Front (Front Pembela Islam/FPI). Other groups, such as the Prosperous Justice Party (Partai Keadilan Sejahtera/PKS) and the Crescent Star Party (Partai Bulan Bintang/PBB), participate in parliamentary democracy to promote Islam. In spite of the differences of articulation, these groups have a common denominator which is their emphasis on the importance of Islam in the public sphere.

Their aspirations for a more Islamic Indonesia have been also channeled through the Indonesian legal system, which is a combination of several legal systems, namely religious law, customary (*adat*) law, and European (civil) law, especially Dutch law that once administered colonial Indonesia. Islamic law is one of Indonesian legal sources that may be incorporated into Indonesian legal system. Several aspects of Islamic law have already been legislated in the state legal system, namely Islamic Family Law (Compilation of Islamic Law/KHI) Based on the Law No. 1 of 1974 on Marriage. When this law was enacted, there was no code that could be referred to by judges. They referred instead to various fiqh sources, creating uncertainty and inconsistency in the decisions which led to turmoil within the Muslim communities. The code on marriage was finally promulgated seventeen years later in the Compilation of Islamic Law (Mulia & Cammack, 2007).

The Law on Religious (Islamic) Courts By the enactment of the Law No. 7 of 1989 on Religious Courts, the position of religious courts was elevated, becoming equal to that of public courts. Previously, religious courts had provisional authority, namely that all their decisions had to be endorsed by public courts (Idri, 2009). The enactment of the Law No. 3 of 2006 on the Amendment of Law No. 7 of 1989 expanded the jurisdiction of the Religious Courts which covers marriage, inheritance, wills (*wasiat*), grants (*hibah*), endowment (*waqf*), Islamic philanthropy (*zakat, infaq* and *sadaqah*), and Islamic economic transactions (Lindsey, 2012). See Lindsey (2012, pp. 263-264).

Zakāt (Islamic alms) Management Law, How *zakat* payments should be regulated has been a consideration of the government since the Dutch Colonial period. After independence, *zakat* was first regulated through Regulation of the Ministry of Religious Affairs No. 4 of 1968 on the establishment of a Board of Amil Zakat. Regarding the development of zakat regulation in Indonesia (Fauzia, 2013). Hajj (pilgrimage) Management Law Based on The Law No. 13 of 2008 on the Pilgrimage Management. *Waqf* (endowment) Law Based on The Law No. 41 of 2004 on *Waqf*. Halal Product Guarantee Law Based on The Law No. 33 of 2014 on Halal Product Guarantee. Sharia Banking Law Based on The Law No. 21 of 2008 on Sharia Banking. Sharia Securities Law Based on The Law No. 19 0f 2008 on Sharia Securities. and Compilation of *Sharīʿa* Economic Law, the amendment of the Law No. 7 of 1989 on Religious Courts with the Law No. 3 of 2006 has given the Religious Courts new authority on Islamic economic dispute resolution. The Compilation of Sharia Economic Law serves as a guide for judges in determining a verdict in Islamic economic disputes. The compilation consists of 845 Articles and divided into four parts (books), namely, 1) Legal Subject and Assets, 2) Contract, 3) *Zakat* and Grant, and 4) Sharia Accounting.

The enactment of these laws passed through many stages which were not always smooth. During the authoritarian rule of the New Order, aspirations for the incorporation Islamic law into the state legal system had been negatively responded by the state. During this period, from 1966 to 1998, the president practically represented the highest authority in Indonesia instead of the People's Consultative Assembly (*Majelis Permusyawaratan Rakyat*). The president's policies were often influenced by his political interests.

The implementation of Islamic laws has raised debates within the Indonesian public space. This is due to diverse views of Indonesian Muslims on particular aspect of state law. For instance, the Compilation of Islamic Law (Kompilasi Hukum Islam/KHI) (Mawardi,

2003; Nurlaelawati, 2010) which had been promulgated by Presidential Instruction (Inpres 1/1991) in 1991 was challenged by the Counter Legal Draft of the Compilation of Islamic Law (CLD KHI) in 2004. Although CLD KHI was drafted by the Working Group of Gender Mainstreaming Unit of the Ministry of Religious Affairs, the initiative was initiated by activists of civil society. In the academic report of the Working Group (Wahid, 2010), it is clearly stated that the CLD KHI was written based on the perspectives of gender, human rights, pluralism, and democracy in the context of Indonesian society. Some points of the existing KHI were regarded to be contradictory to those principles. For instance, while polygamy is allowed in the KHI, it is prohibited (*harām li ghairih)* in the CLD KHI.

In addition to the incorporation of Islamic laws, another way to institutionalize Islamic laws in the state's legal system is by enacting Islamic bylaws in local governments (Hooker, 2008; Salim, 2008). Since the issuance of the Law No. 22 of 1999 on Regional Autonomy, many regions have proposed Islamic bylaws, such as *zakāt* bylaws, Islamic dress bylaws, zero-alcohol zone bylaws, and the prohibition of "immorality" bylaws. The enactment of these Islamic bylaws in regional level has raised varied reactions from society.

In 2003, teachers of East Lombok region rejected the East Lombok *zakāt* regional regulation, which automatically deducted the alms-tax from the teachers' monthly salary for management by the local government. The policy was viewed as a violation to their rights; fulfilling the teachings of *zakāt* should not be imposed, but should be based on what they believe (Aniq, 2012). The enactment of Islamic bylaws is also viewed as political and discriminative. For instance, the obligation for women to wear veils, the prohibition for women from being outside the home at night, and the restriction to the minorities' rights. Ironically, in some cases, local authorities whose regions implement Islamic bylaws have been proven to have committed corruption. The arrest of the regent of the Cianjur region who was proven to have committed corruption is an example. This regent was known to always encourage his citizens to conduct their morning prayers (*subh*) in congregation (Sudrajat, 2018).

Ideas on the Institutionalization of Islamic Economics in Indonesia

The construction of the Indonesian Islamic economic rules is inseparable from the historical development of Indonesians' understanding of the Sharia-compliant Economy. Since the pre-independence of Indonesia, Islamic economics has been seriously discussed among Muslim intellectuals in *Nusantara*, the Indonesian archipelago.

Mohammad Hatta, an economist and the first vice president of Indonesia, wrote several articles on economic issues in relation with Islam, where he discusses the concept of bank interest and usury. Hatta argues that interest is not identical with usury, because loans given on interest are used for productive purposes. According to Hatta, bank interest is similar to usury only in the context of consumptive kredit (Rahardjo, 1999). In the 1950s, the Minister of Finance, Syafruddin Prawiranegara, was of the same opinion as Hatta. According to Syafruddin, while *ribā* is a transaction that entails extortion and fraud, credit transactions in modern banking are kinds of trade. It is not *ribā*. Bank interest can be usury if the interest is set too high and imposed on the borrower.

The notion on bank interest and usury was not only discussed by the early Indonesian economists, but also by '*ulamā*. One of the '*ulamā* whose legal thought was progressive in his time was Ahmad Hassan, the chairman of Islamic Union (*Persatuan Islam*/PERSIS) an Islamic organization based in Bandung. Hassan argued in his work on usury that bank interest is not in itself usurious. Rather, it could become a form of usury depending on the level and system of interest used. If the interest rate is doubled (*ad'āfan mudā'afan*) such as the interest rate of loan sharks, then it is forbidden. However, if the interest rate is not exploitative, it is not usurious and therefore acceptable in Islamic law (Mubarok, 2004).

In addition, the two largest Islamic organizations in Indonesia, Nahdhatul Ulama (NU) and Muhammadiyah, viewed bank interest as *mutashābihāt,* meaning that it was neither *halal* nor *harām*. This view was based on the argument that the existence of conventional banks and the interest imposed on debtors and given to depositors was needed for the economic growth of the Muslim community. NU released its religious ruling (*fatwā*) in 1957, while Muhammadiyah issued their own in 1968. Thirty-five years later in 2003, the '*Ulamā* Council of Indonesia (Majelis Ulama Indonesia/MUI), whose members are from various Indonesian Muslim organizations, issued a different *fatwā*. They ruled that bank interest is usury and is thus *haram* (Mubarok, 2006).

In the Guided Democracy Regime (Demokrasi Terpimpin, from 1959 to 1965), the discussion on the relationship between Islam and the economy was limited to the issue of bank interests. The discussion did not go into greater depth because any discussion about Islamic economic system would soon be associated with separatist efforts in establishing an Islamic state.

In the New Order era, from 1965 to 1998, freedom of expression was relatively more open. In the late 1970s, a number of books related to Islamic economics began to be

translated and published. According to (Rahardjo, 1999), one of the most important factors in the development of thought on Islam and economics was the Third East Coast Regional Conference, organized by the Muslim Student Association of USA and Canada in April 12-14, 1968 in Holiday Hills, Pawling, New York. At the conference, Islamic economic theories were discussed (*Proceedings of the Third East Coast Regional Conference*, 1968). Indonesians were among the attendees of this conference, the most notable of whom was A. M. Saefuddin. When Saefuddin returned to Indonesia, he spread his new-found ideas on Islamic economics in Indonesian universities.

At the time, the economic system implemented in Indonesia was billed as an alternative economic system, the so-called *Pancasila* Economic System. This system absorbed economic notions from various systems, including the liberal and socialist models. The development of an Islamic economic system was intended by sharia economic activists to contribute to filling the gaps in the Pancasila Economic System, not to replace it (Rahardjo, 1999).

State-Designed Sharia-compliant Economic Rule in the New Order Era

Compared to Islamic family law, which was enacted in 1974 (Azra, 2003), Islamic economic law was promulgated later. The birth of Sharia-based financial systems began in 1983 when the December 1983 Legislative Package (Pakdes 83) was released containing a number of regulations in the banking sector. One of the rules is that banks were allowed to provide loans with interest of 0% (zero interest). This was a milestone in the commencement of interest-free banking. The existence of Pakdes 83 was strengthened by the issuance of the Law No. 7 of 1992 concerning Banking. Since then, the Indonesian banking industry has juridically recognized the profit-sharing system.

Substantially, Law No. 7 of 1992 regulates conventional banks more than banks with the profit-sharing principles. The use of "Islamic bank" or "Sharia bank" terms was avoided at that time in order to anticipate negative response of secular nationalist groups, In 1970s, the efforts to establish Islamic banking failed. That was due to the government's suspicion of the Darul Islam and Negara Islam Indonesia (DI/TII) separatist movements. The official statement of the government to refuse the idea was the lack of laws that ruled interest-free banking. In the Law No 14 of 1967 on Principles of Banking, it was stated that every credit transaction must be done with interest (Rahardjo, 1999). Thus, in article 1.12 of the law, it is stated that banks may operate based on the principle of profit-sharing.

Furthermore, even though Law No. 7 of 1992 allowed banks to operate based on the principle of profit-sharing, there was no further direction regarding how the new system should be run. Therefore, to provide clear understanding and guidance, the government issued the Government Regulation (*Peraturan Pemerintah*/PP) No. 72 of 1992 Concerning Banks based on profit sharing principles. According to article 1.1 of the Government Regulation, what is meant by a bank based on the principle of profit-sharing is a Commercial Bank or People's Credit Bank that conducts business activities solely based on the principle of profit-sharing. The article implies that the term "bank with a profit-sharing system" is the principal terminology used for Islamic or Sharia banks.

Profit-sharing in Islamic transaction law (*fiqh mu'āmala*) is called *mudaraba*. It denotes a transaction in which an investor (*mudarib*) hands over capital (*ra's al-māl*) to an entrepreneur (*al-'āmil*) to work with. The profits are shared with an agreed percentage (ratio/*nisba*) of net profit (*al-ribh*). In *mudaraba*, both parties are likely to profit or suffer loss together. If there is a loss, the investor's capital decreases and the entrepreneur gets nothing.

However, the Sharia bank in its operation does not merely use the principle of profit sharing, but also applies traditional Islamic contracts commonly referred to as Sharia principles, such as *murābaha* (cost plus finance)*, mushāraka* (joint venture)*, wadī'a* (safekeeping)*, ijār* (leasing), *hiwala* (an international fund transfer system), *takāful* (Islamic insurance), and *sukūk* (Islamic bonds). These instruments replace the conventional bank system in the form of interest (*ribā*), uncertainty (*gharār*), and gambling (*maisir*) which are prohibited in Islam.

The enactment of Banking Law No. 7 of 1992 became the operational basis of Bank Muamalat Indonesia (BMI), the first Sharia bank in the country which was established in 1991. The establishment of BMI reflected changes in Indonesia's political and cultural climate. By its supporters, it was regarded as a symbol of the awakening of Islamic economics. Since the Indonesian economy was dominated by Chinese conglomerates, the establishment of BMI was also considered as addressing the economic inequality in the country (Hefner, 2003). A symbolization of a certain moment can be politically significant. It can be used as a cohesive power for a specific goal (Eickelman & Piscatori, 2004).

The enactment of Islamic economic law and the establishment of the first Sharia financial institutions in Indonesia were predominantly influenced by a strategic transition in President Suharto's New Order regime during the late 1980s. Suharto rose to power with full military support. He was one of the top military generals and successfully crushed the

Indonesian Communist Party (PKI) movement in 1965. For decades, the government had a secular-nationalist view that marginalized political Islam. However, when support from the military which lasted until the late 1980s weakened, Suharto then turned to seek political support from Muslims. In the beginning of 1990s, Suharto started a policy of "re-Islamization" to gain political legitimacy among the growing Muslim middle class and intellectual circles (Dahlan et al., 2024). Moreover, the 1988 banking deregulation, known as Pakto 88, made this shift happen even faster by making new financial models possible. The success of Islamic Development Bank's globally also convinced Indonesian policymakers that Sharia principles could work with and help the country's economic growth (Zulkarnain & Arif, 2025).

Suharto played a crucial role in accommodating the aspirations of these educated Muslims and facilitating the establishment of the Association of Indonesian Muslim Intellectuals (ICMI), an organization led by B.J. Habibie, which served as a leading advocate for Islamic economic integration through a top-down political approach. Furthermore, Suharto gave his full backing for the establishment of Bank Muamalat Indonesia (BMI). Through his foundation, Yayasan Amal Bhakti Muslim Pancasila, he lent funds for the bank's initial deposit. Suharto also made personal appeals to important figures to invest in BMI. The first Islamic banking was finally launched on May 15, 1992, in Jakarta (Saeed, 2008).

The policy to approve the incorporation of Islamic economic law into state legal system was motivated by his overtures to the Muslim community as a political block at a time when military support for his regime was weakening (Hefner, 2003). By embedding these rules into the legal framework of the state, he effectively utilized Islamic economics as a tool of political consolidation. Suharto's political strategy of accommodation in the early 1990s was a calculated move that kept the New Order relevant in Indonesia's changing socio-political landscape (Effendy, 2003; Hefner, 2000; Liddle, 1996).

In line with this argument, Tarek Masoud through his political economy framework suggests that authoritarian rulers tend to adopt religious policies not necessarily out of personal conviction, but as a calculated way to suppress political opponents and embrace new mass bases when their old ones drift away (Masoud, 2013). This pattern was reflected in the above case when Suharto's fractious relationship with the military prompted him to approach the Muslim middle class as a new source of support. The establishment of ICMI and BMI was seen as a strategy to bring opposition groups into the circle of power to maintain control. Thus, the enactment of Islamic economic law was a regime's strategy to

meet the expectations of Muslim professionals and to make any new economic power remained under the regime's control. (Masoud, 2013).

CONCLUSION

The secularist expectation that for a modern state to succeed, religion should be marginalized into purely private domain does seem to take hold in Indonesia. The *Pancasila* as the foundation of the state, being neither secular nor religious-based, seem to have bestowed the right for Indonesian people to propose particular aspects of Islamic law to be incorporated into the state legal system. Due to this close but ambiguous relationship between religion and the state, there have always been demands to institutionalize Islamic teachings in all aspects of Indonesian Muslims' lives. One of the ways to cope with the demands legally is by incorporating Islamic law into the Indonesian legal system.

In Indonesia, there are several Islamic laws which have been enacted as state law, one of which is the Sharia-based economic rule. This was the result of long efforts by proponents of the law before it was ratified by the state. Nevertheless, the enactment and implementation of the rule were driven primarily by Suharto, the nation's autocrat, as a means of ensuring his political survival. This study demonstrates that the promulgation of Sharia-compliant rules was not merely a response to public demand, but a calculated intersection between religious aspirations and the New Order regime's interest in maintaining dominance. Consequently, the establishment of Islamic financial institution served as a form of state diplomacy aimed at perpetuating the regime's power during a period of shifting alliances. Specifically, Suharto turned to this new economic framework to cultivate legitimacy among the growing educated Muslim middle class and to create a strategic counterweight against declining support from the military.

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