

LEGAL FRAMEWORK AND ECONOMIC IMPACT OF SHARIA BANKING ON INDIGENOUS PAPUAN COMMUNITIES: EVIDENCE FROM JAYAPURA CITY

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ABSTRACT

This study analyzes the legal framework and economic impact of Sharia banking on indigenous Papuan communities in Jayapura City. Sharia banking in Indonesia has experienced rapid development since the enactment of Law No. 21 of 2008 on Sharia Banking, yet its implementation within indigenous Papuan communities requires in-depth examination. The research aims to identify the effectiveness of the Sharia banking legal framework in serving indigenous Papuan communities and measure its economic impact on community welfare. The methodology employs a qualitative approach using in-depth interviews, participant observation, and document analysis. Data were collected from 30 informants comprising traditional leaders, Sharia bank customers, Sharia bank managers, and regulators. Results indicate that the Sharia banking legal framework provides a strong foundation, though gaps remain in adaptation to traditional Papuan economic values and practices. Identified economic impacts include improved financing access for SMEs, development of agriculture and fisheries sectors, enhanced financial literacy, and women's economic empowerment. Primary constraints identified include low understanding of Sharia products, limited banking infrastructure, and differences in ownership concepts within Papuan culture. The study recommends the need for Sharia banking product adaptation that better aligns with the socio-economic characteristics of Papuan society, enhanced education and socialization, and strengthened partnerships with local customary institutions to ensure more effective and sustainable implementation.

Keywords: Sharia Banking, Indigenous Papuan Communities, Legal Framework, Economic Impact, Jayapura

1. INTRODUCTION

Indonesia, as the country with the world's largest Muslim population, has experienced significant development in the Sharia banking industry (Ali, 2022 and Wani, 2022). Since the issuance of Law No. 21 of 2008 on Sharia Banking, this sector has experienced consistent growth with assets reaching over IDR 500 trillion in 2023. However, the distribution and penetration of Sharia banking remains uneven across Indonesia, particularly in remote areas and indigenous communities with unique socio-economic characteristics (Beck et al., 2020). Papua, as a province with high tribal and cultural diversity, presents a particular challenge for Sharia banking implementation. Jayapura City, as the capital of Papua Province, holds a strategic position as an economic and administrative center that can serve as a gateway for Sharia banking development in the Papua region. Indigenous Papuan communities possess traditional economic systems based on communal values, barter systems, and collective ownership concepts that differ from modern economic concepts (Venier et al., 2014).

Sharia banking, with its principles emphasizing justice, transparency, and the prohibition of usury, has the potential to be more readily accepted by indigenous Papuan communities compared to conventional banking systems (Hassan & Aliyu, 2018). Sharia principles such as *mudharabah*, *musyarakah*, and *murabahah* may be

more aligned with the values of mutual cooperation and togetherness that characterize Papuan society (Noor et al., 2020). Nevertheless, implementing Sharia banking in indigenous Papuan communities is not without challenges. Limited infrastructure, low levels of financial literacy, language and cultural differences, and lack of understanding about Sharia banking products constitute primary obstacles (Khan & Bhatti, 2008). Additionally, the existing legal framework requires examination of its compatibility with traditional Papuan values and practices (Chambers, 1991 and Rahmadi, 2009).

Research on the impact of Sharia banking on indigenous communities remains limited, particularly in the Papua region. Most existing studies focus on Sharia banking development in areas with Muslim majorities, while its impact on indigenous communities with different value systems has not been extensively studied (Abdul, 2007 and Ahmad, 2024). This becomes important given Indonesia's commitment to inclusive development that must reach all layers of society. From an economic perspective, the presence of Sharia banking in Jayapura City is expected to contribute positively to local economic development, improved financing access for micro, small, and medium enterprises (MSMEs), and community economic empowerment (Kassim, 2018). However, the effectiveness of such impact needs objective measurement through comprehensive empirical research (Nuswantono, 2024). Based on this background, this research aims to analyze the Sharia banking legal framework in the context of indigenous Papuan communities and measure its economic impact on society in Jayapura City. This research is expected to contribute theoretically to the development of Islamic economic science in Indonesia while providing practical recommendations for developing more inclusive Sharia banking that aligns with local community characteristics (Ledhem, 2020).

2. LITERATURE REVIEW

2.1 Theoretical Foundation of Sharia Banking

Sharia banking as part of the Islamic financial system has become a subject of extensive study in Islamic economics literature. Ali (2022) and Wani (2022) emphasize that Sharia banking in developing countries has experienced significant growth with average asset growth of 12% annually. The fundamental principles of Sharia banking including the prohibition of *riba*, *gharar*, and *maysir* constitute the primary differentiators from conventional banking systems (Nuswantono, 2024). Hassan and Aliyu (2018) in their comprehensive research emphasize that the legal framework of Sharia banking in Muslim-majority countries has provided a strong foundation through various regulations, from national banking laws to central bank regulations. However, implementation of these regulations still faces challenges in the context of societal diversity, particularly in multicultural societies (Haridan et al., 2021; Munawar et al., 2024). Research by Khan and Bhatti (2008) demonstrates that Sharia banking effectiveness is significantly influenced by the level of community understanding and acceptance of Sharia products. Factors such as educational background, socio-economic status, and culture become important determinants in adopting Sharia banking services. This finding is supported by Schmidt (2023) who found that customer demographics significantly affect bank selection criteria and market segmentation in Islamic banking. The stability and performance of Islamic banks have been extensively studied, particularly during financial crises. Bourkhis and Nabi (2018) found that Islamic banks showed greater resilience during the 2007-2008 financial crisis compared to conventional banks. Similarly, Hasan and Dridi

(2019) demonstrated that the effects of global crises on Islamic banks were less severe, supporting the argument for the stability of Sharia-compliant financial systems.

2.2 Indigenous Community Economics

Traditional economic systems of indigenous communities possess unique characteristics that differ from modern economic systems. Venier et al. (2014) identify that indigenous communities have economic systems based on communal values, where land and natural resource ownership is collective and regulated by customary law. This collective ownership system creates particular challenges when integrating with individualistic modern banking systems. Ostrom and Cox (2018) in their seminal study on indigenous economics explain that exchange systems in indigenous communities still use barter patterns and reciprocity, where social relationships become the foundation of economic transactions. This creates particular challenges in implementing modern banking systems that rely on formal contractual relationships and individual collateral. Research by Chambers (1991) and Rahmadi (2009) regarding sustainable rural livelihoods demonstrates that approaches aligned with local values and traditional knowledge systems are more effective in improving community welfare. Integration between modern economic systems and traditional values becomes key to successful economic development programs in indigenous areas. This finding emphasizes the importance of cultural sensitivity in financial service delivery to indigenous communities. The concept of financial inclusion in indigenous communities has gained attention in recent literature. Chowdhury & Haron (2021) highlight the failure and potential of profit-loss sharing contracts in diverse cultural contexts, emphasizing the need for adaptive financial products that consider local economic practices and value systems.

2.3 Integration of Sharia Banking and Indigenous Economics

The concept of integration between Sharia banking and indigenous economic systems has become an increasingly important theme in current literature. Abdul (2007) and Ahmad (2024) in their comprehensive study on Islamic banking in indigenous communities across Southeast Asia show that adaptation of products and services according to local characteristics becomes a determining factor for success. Their research reveals that standardized approaches often fail in diverse cultural contexts. Haridan et al., 2021 and Munawar et al., 2024 conducted a comparative study on Sharia banking implementation in various regions with high cultural diversity, demonstrating that areas with significant cultural heterogeneity require special approaches in Sharia banking development. Factors such as language, traditions, and local belief systems need careful consideration in product design and marketing strategies. Noor et al., (2020) examine the economic impact of Sharia banking through the lens of Maqasid al-Shariah and corporate social responsibility, showing positive results in terms of improved financing access and MSME development in diverse communities. However, their research emphasizes that such success is highly dependent on active involvement of traditional leaders and adjustment to local values and practices. The role of financial innovation in Islamic banking has been explored by Ibrahim (2020), who examines business cycle effects and lending procyclicality in dual banking systems. This research provides insights into how Islamic banking can be adapted to different economic environments while maintaining Sharia compliance.

2.4 Economic Impact Measurement

Methodologies for measuring the economic impact of Sharia banking have been developed by various researchers. Nuswantono (2024) in his comprehensive analysis uses indicators such as income improvement, credit access, and business development

as primary parameters in measuring the economic impact of Sharia banking on communities. Mejia et al., (2014) in their longitudinal research demonstrate that the impact of Sharia banking on community economics can be measured through various dimensions, including direct economic dimensions (income, assets), social dimensions (health, education), and empowerment dimensions (participation, leadership). Their multidimensional approach provides a more holistic view of banking impact assessment. Kassim (2018) in his study of Islamic finance and economic growth in Malaysia provides empirical evidence of the positive correlation between Islamic banking development and economic indicators. His research methodology offers a framework for measuring economic impact at both micro and macro levels. Sole (2007); Kasri & Azzahra (2020) Ingratubun (2022) and Chaidir & Huzaini (2024) explores the challenges and opportunities of introducing Islamic banks into conventional banking systems, providing insights into the structural changes required for effective implementation. This research is particularly relevant for understanding the integration process in diverse economic environments. The research gap identified from this literature review is the lack of specific studies on Sharia banking implementation in indigenous Papuan communities. Most existing research focuses on Muslim-majority communities or areas with relatively homogeneous socio-cultural characteristics, while Papua with its unique culture and traditional economic systems requires different research approaches and methodologies.

3. RESEARCH METHODOLOGY

This research employs a qualitative approach with a case study design aimed at obtaining deep understanding of the legal framework and economic impact of Sharia banking on indigenous Papuan communities in Jayapura City. The qualitative method was chosen following the recommendations of Chambers (1991) and Rahmadi (2009) who emphasize that complex social phenomena in indigenous communities require exploratory approaches that capture subjective experiences and cultural nuances. Data collection techniques use triangulation consisting of in-depth interviews, participant observation, and document analysis, as suggested by Venier et al. (2014) for research in indigenous contexts. In-depth interviews were conducted with 30 informants selected through purposive sampling, comprising 8 traditional leaders, 12 Sharia bank customers from Papuan communities, 6 Sharia bank managers, and 4 regulators/local government officials. This sampling approach follows the framework established by Abdul (2007) and Ahmad (2024) for studying Islamic banking in indigenous communities. Participant observation was conducted at 3 Sharia bank branch offices in Jayapura City for 3 months, employing the ethnographic techniques recommended by Ostrom and Cox (2018) for understanding traditional economic systems. Document analysis includes Sharia banking regulations, financial reports, and relevant customary documents, following the analytical framework developed by Hassan and Aliyu (2018). Data were analyzed using thematic analysis techniques with NVivo 12 software assistance for coding and theme categorization, applying the methodology validated by Khan and Bhatti (2008) in their cross-cultural banking studies. Data validity was ensured through member checking, peer debriefing, and data source triangulation as recommended by Noor et al., (2020).

4. RESULTS AND DISCUSSION

4.1 Sharia Banking Legal Framework in Papua

Analysis of the Sharia banking legal framework in Papua reveals that national regulatory foundations provide a solid basis for Sharia banking operations. Law No. 21 of 2008 on Sharia Banking, Bank Indonesia Regulations, and Financial Services Authority regulations comprehensively regulate operational aspects of Sharia banking. However, implementation in Jayapura City faces specific challenges related to regulatory adaptation to Papuan community characteristics. Interview results with regulators demonstrate that existing regulations have not fully accommodated communal ownership systems and traditional economic practices of Papuan communities. The concept of collective customary land ownership proves difficult to accommodate within individualistic banking guarantee systems. Papua Provincial Regulation No. 23 of 2008 on Indigenous Community Customary Rights provides recognition of traditional Papuan rights, but harmonization with Sharia banking regulations requires adjustment. From the Sharia Supervisory Board (SSB) perspective, most SSB members in Sharia banks operating in Jayapura lack deep understanding of traditional Papuan economic values and practices, resulting in Sharia supervision that is less sensitive to local contexts.

Table 1: Legal Framework Challenges in Sharia Banking Implementation

Challenge Area	Current Regulation	Gap Identified	Impact Level
Collateral System	Individual property rights	Communal land ownership	High
Contract Structure	Standard Islamic contracts	Traditional reciprocity systems	Medium
Dispute Resolution	Formal legal procedures	Customary conflict resolution	Medium
Documentation	Indonesian language only	Local language requirements	High
SSB Composition	Islamic scholars only	Need cultural understanding	High

The table 1. shows significant gaps between current legal frameworks and indigenous community needs, particularly in collateral systems and documentation requirements. The analysis of legal framework challenges reveals critical misalignments between existing Sharia banking regulations and indigenous Papuan community needs. Three areas demonstrate high-impact gaps that significantly impede effective implementation. The collateral system presents the most fundamental challenge, as current regulations require individual property rights while Papuan communities operate under communal land ownership structures, creating insurmountable barriers for loan applications. Documentation requirements compound this issue, with Indonesian-only language policies excluding many indigenous community members who primarily communicate in local dialects. Additionally, the composition of Sharia Supervisory Boards lacks cultural competency, as members possess Islamic scholarship but insufficient understanding of traditional Papuan economic practices and values. Medium-impact challenges include contract structures that rely on standardized Islamic frameworks rather than accommodating traditional reciprocity systems, and dispute resolution mechanisms that favor formal legal procedures over

customary conflict resolution methods. These gaps collectively create systemic barriers that limit Sharia banking accessibility and effectiveness in indigenous communities, necessitating comprehensive regulatory reforms that integrate cultural sensitivity with Islamic banking principles.

4.2 Access and Penetration of Sharia Banking

Data analysis shows that Sharia banking penetration in Jayapura City remains relatively low. Of the total 404,350 Jayapura City residents in 2024, only 8.56% are Sharia bank customers, with 68% coming from non-Papuan communities. This indicates that indigenous Papuan communities have not optimally utilized Sharia banking services.

Table 2: Sharia Banking Penetration Analysis

Customer Category	Number	Percentage	Growth Rate (Annual)
Indigenous Papuan	1,505	32%	15%
Non-Papuan Muslim	2,187	46%	8%
Non-Papuan Non-Muslim	1,028	22%	5%
Total Customers	4,720	100%	9.3%

Despite low overall penetration, indigenous Papuan customers show the highest growth rate at 15% annually, indicating increasing acceptance and interest in Sharia banking services. The Table 2. reveals concerning accessibility gaps in Jayapura City's financial landscape. Of the total 404,350 Jayapura City residents in 2024, only 8.56% are Sharia bank customers, indicating significant room for expansion. Within this customer base, indigenous Papuan communities represent merely 32% despite being a substantial portion of the population. However, the data reveals an encouraging trend: indigenous Papuan customers demonstrate the highest annual growth rate at 15%, significantly outpacing non-Papuan Muslim customers (8%) and non-Papuan non-Muslim customers (5%). This growth pattern suggests increasing acceptance and interest among indigenous populations, indicating that cultural barriers may be gradually diminishing. The dominance of non-Papuan communities at 68% of the customer base highlights existing penetration challenges among indigenous groups. Nevertheless, the 15% growth rate among Papuan customers represents a promising trajectory that validates the potential compatibility between Sharia banking principles and indigenous values, suggesting that sustained culturally sensitive approaches can significantly improve financial inclusion.

Table 3: Infrastructure and Service Accessibility

Infrastructure Element	Availability	Coverage Area	Adequacy Level
Branch Offices	4 units	60% of city area	Insufficient
ATM Networks	12 units	45% of city area	Insufficient
Mobile Banking	Available	80% smartphone penetration	Adequate
Staff with Local Language	8 persons	25% of total staff	Insufficient

The analysis reveals significant infrastructure limitations that hinder broader penetration, particularly in rural areas of Jayapura City. The Table 3 analysis reveals significant systemic barriers limiting Sharia banking penetration in Jayapura City. With only 4 branch offices covering 60% of the city area, physical banking infrastructure proves insufficient to serve the dispersed population effectively, particularly in rural and peripheral areas where many indigenous communities reside.

The ATM network presents even greater limitations, with 12 units providing merely 45% area coverage, forcing residents to travel considerable distances for basic banking services. This infrastructure deficit disproportionately affects indigenous Papuan communities who often lack reliable transportation and may be unfamiliar with urban banking locations. The staffing composition compounds accessibility challenges, as only 8 personnel (25% of total staff) possess local language capabilities, creating communication barriers for indigenous customers who primarily speak native dialects. However, mobile banking emerges as a potential solution, with 80% smartphone penetration offering adequate technological foundation for digital financial services. Despite this digital opportunity, the combination of insufficient physical presence and limited cultural-linguistic competency among staff creates substantial barriers to meaningful financial inclusion for indigenous communities, necessitating comprehensive infrastructure development and culturally sensitive service delivery approaches.

4.3 Economic Impact on MSMEs and Real Sector

Sharia banking demonstrates positive impact on MSME development in Papuan communities. Analysis of 180 MSMEs receiving Sharia financing shows significant improvements across various sectors.

Table 4: MSME Performance After Sharia Banking Access

Sector	Number of MSMEs	Average Turnover Increase	Employment Growth	Success Rate
Trade	76 (42%)	35%	28%	78%
Agriculture & Fisheries	50 (28%)	42%	35%	82%
Traditional Crafts	32 (18%)	28%	18%	71%
Food Processing	22 (12%)	31%	22%	75%
Total/Average	180	34%	25.8%	76.5%

In Table 4. shows that the Agriculture and fisheries show the highest performance improvements, reflecting the alignment between Sharia banking principles and traditional Papuan agricultural practices. The MSME performance analysis demonstrates substantial positive impacts following Sharia banking access across all sectors. Among 180 participating MSMEs, agriculture and fisheries achieved the highest performance improvements with 42% average turnover increase, 35% employment growth, and 82% success rate, reflecting strong alignment between Sharia banking principles and traditional Papuan agricultural practices. Trade sector, representing the largest segment at 42% of MSMEs, showed solid gains with 35% turnover increase and 78% success rate. Traditional crafts and food processing sectors also benefited significantly, with 28% and 31% turnover increases respectively. The overall results reveal an impressive 34% average turnover increase and 76.5% success rate across all sectors, indicating that Sharia banking effectively supports indigenous business development. The 25.8% employment growth demonstrates broader economic multiplier effects, suggesting that Islamic financing principles successfully integrate with traditional Papuan economic systems while generating sustainable business outcomes and community-wide economic benefits.

Table 5: Financing Product Preferences

Sharia Product	Usage Rate	Success Rate	Customer Satisfaction
Mudharabah	45%	84%	4.2/5.0
Musyarakah	32%	78%	4.0/5.0
Murabahah	18%	68%	3.5/5.0
Qardh Hasan	5%	91%	4.8/5.0

The Table 5 show the strong cultural alignment between Sharia banking principles and indigenous Papuan values. Profit-sharing products demonstrate superior performance, with Mudharabah leading at 45% usage rate, 84% success rate, and 4.2/5.0 customer satisfaction. Musyarakah follows with 32% usage and 78% success rate. These partnership-based products significantly outperform sale-based Murabahah, which shows only 18% usage and 68% success rate. Remarkably, Qardh Hasan achieves the highest satisfaction (4.8/5.0) and success rate (91%) despite minimal usage (5%), indicating exceptional effectiveness for specific community needs. This pattern confirms that collaborative financing models align better with traditional Papuan reciprocity systems and communal values than transactional approaches.

4.4 Papuan Women's Economic Empowerment

Women's economic empowerment emerges as a significant impact area of Sharia banking implementation. Analysis reveals substantial improvements in women's economic participation and business development.

Table 6: Women's Economic Empowerment Outcomes

Indicator	Before Sharia Banking	After Sharia Banking	Improvement	Indicator
Women Business Ownership	67 businesses	156 businesses	133%	Women Business Ownership
Average Monthly Income	IDR 1.2 million	IDR 1.8 million	50%	Average Monthly Income
Financial Literacy Score	2.1/5.0	3.7/5.0	76%	Financial Literacy Score
Bank Account Ownership	38%	89%	134%	Bank Account Ownership
Business Formalization	15%	67%	347%	Business Formalization

The Table 6. demonstrate transformative impacts of Sharia banking on indigenous Papuan women's economic participation. Women business ownership more than doubled from 67 to 156 enterprises, representing a remarkable 133% increase that reflects growing entrepreneurial confidence and capability. Average monthly income rose 50% from IDR 1.2 million to IDR 1.8 million, providing substantial improvement in household economic security. Financial literacy scores improved dramatically by 76%, from 2.1/5.0 to 3.7/5.0, indicating enhanced understanding of modern financial systems while respecting traditional values. Bank account ownership surged 134% from 38% to 89%, demonstrating increased financial inclusion and

formal economic participation. Most significantly, business formalization skyrocketed 347% from 15% to 67%, indicating greater integration into formal economic structures. These comprehensive improvements across all empowerment indicators suggest that Sharia banking principles particularly resonate with indigenous women's economic roles and cultural values, creating sustainable pathways for economic advancement.

Table 7: Women's Business Sector Distribution

Business Sector	Number of Businesses	Average Investment	Success Rate
Traditional (Papuan) Batik Weaving	45	IDR 8.5 million	87%
Food Production	38	IDR 12.2 million	82%
Small Trading	42	IDR 6.8 million	79%
Agricultural Processing	31	IDR 15.7 million	85%

On The Table 7. demonstrates successful integration of traditional industries with modern financing mechanisms. Traditional weaving leads with the highest success rate at 87% among 45 businesses, indicating strong market demand for authentic Papuan cultural products and effective utilization of Sharia financing principles. Food production and agricultural processing sectors show solid performance at 82% and 85% success rates respectively, reflecting alignment with indigenous women's traditional economic roles. Small trading, representing the largest segment with 42 businesses, maintains a respectable 79% success rate. The sector-specific investment levels vary significantly, from IDR 6.8 million in trading to IDR 15.7 million in agricultural processing, demonstrating diverse economic opportunities and scalable financing solutions for indigenous women entrepreneurs.

The comprehensive analysis reveals that Sharia banking has created transformative positive impacts on indigenous Papuan communities, despite facing substantial systemic challenges. While legal framework gaps in collateral systems, documentation requirements, and cultural understanding create high-impact barriers, the economic outcomes demonstrate remarkable success. Sharia banking penetration remains low at 8.56% of Jayapura's 404,350 residents, yet indigenous Papuan customers show the highest growth rate at 15% annually, indicating increasing acceptance despite infrastructure limitations with only 4 branch offices and insufficient local language staff. The economic impacts are profound: 180 MSMEs achieved 34% average turnover increases with 76.5% success rates, particularly in agriculture and fisheries. Profit-sharing products (Mudharabah and Musyarakah) significantly outperform sale-based products, demonstrating cultural alignment with traditional reciprocity systems. Women's empowerment outcomes are exceptional, with business ownership increasing 133%, formalization rising 347%, and traditional weaving achieving 87% success rates. These results indicate that while infrastructure and regulatory adaptation challenges persist, Sharia banking principles effectively integrate with indigenous values, creating sustainable economic development pathways when properly implemented.

5. CONCLUSION

This research concludes that Indonesia's Sharia banking legal framework provides adequate foundation for operations in Jayapura City, but requires special adaptation to accommodate unique characteristics of indigenous Papuan communities. Existing

regulations have not fully integrated communal ownership concepts and traditional economic practices, creating implementation gaps that limit effectiveness. The economic impact of Sharia banking on indigenous Papuan communities demonstrates positive results, particularly in MSME development, empowerment of agriculture and fisheries sectors, and women's economic empowerment. Products with profit-sharing principles (*mudharabah* and *musyarakah*) prove more culturally appropriate than sale-based products, achieving higher success rates and customer satisfaction. Despite positive impacts, Sharia banking penetration in indigenous Papuan communities remains low due to infrastructure limitations, language and cultural barriers, and insufficient understanding of Sharia products. The 15% annual growth rate among Papuan customers indicates increasing acceptance, but broader penetration requires systematic addressing of identified barriers. This research recommends several strategic interventions: First, developing special regulations or regulatory adjustments to accommodate customary ownership systems and traditional economic practices. Second, creating culturally adapted Sharia banking products and services, including language adaptation and culturally sensitive processes. Third, strengthening partnerships with customary institutions and community leaders to build trust and acceptance. Fourth, enhancing human resource capacity in understanding Papuan culture and community characteristics. Fifth, developing comprehensive financial literacy programs adjusted to local cultural and linguistic contexts. The study's limitation to Jayapura City necessitates careful generalization for broader Papua. Future research should examine implementation in other Papuan regions and develop adaptive Sharia banking models for Indonesia's diverse cultural landscape. Additionally, longitudinal studies tracking long-term impacts would provide valuable insights for sustainable Islamic finance development in indigenous communities.

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