Proceedings of The 3rd International Conference on Science and Islamic Studies
ISSN: 3024-9058 (Online - Elektronik)
Volume: 3, 2025
Publisher: Program Pascasarjana, UIN Alauddin Makassar

ANALYSIS OF CHALLENGES AND OPPORTUNITIES IN THE DEVELOPMENT OF SHARIA FINANCIAL INSTITUTIONS INTEGRATED WITH THE NORTH MALUKU SME ECOSYSTEM

Sudin Yamani[1]

[1]Institut Agama Islam Negeri Ternate, Indonesia
Correspondence Email: sudinyamani0@gmail.com

ABSTRACT

The development of Islamic financial institutions (IFIs) integrated with the micro, small, and medium enterprise (UMKM) ecosystem is an important strategy in promoting financial inclusion and sustainable regional economic growth. This study aims to analyze the challenges and opportunities in developing LKS integrated with the UMKM ecosystem in North Maluku, as well as to formulate a contextual integration model that is in line with the socio- economic characteristics of the archipelago. This study uses a qualitative approach with a descriptive design through in-depth interviews, field observations, and documentation studies. Research informants include Islamic financial institution leaders, MSME actors, practitioners, and Islamic economics academics. Data analysis was conducted using thematic analysis through the stages of open coding, axial coding, and selective coding. The results show that the integration of LKS-UMKM in North Maluku faces various structural challenges, including low Islamic financial literacy, limited administrative capacity of UMKM, internal readiness of LKS, regulations that are not in line with local informal and seasonal economic practices, and uneven access to digital technology due to the geographical conditions of the archipelago. On the other hand, opportunities for integration are wide open in line with the dominance of the fisheries and traditional trade sectors, government policy support, increased public acceptance of the Islamic economy, developments in digital technology, and the potential for cross- sector collaboration. Based on these findings, this study formulates a contextual sharia integration model that relies on the synergy of sharia literacy, structured business assistance, financing product innovations that are in line with local business characteristics, and inclusive digitalization. This model emphasizes that the success of LKS-UMKM integration is determined by multi-stakeholder ecosystem interactions and adaptation to the local context, thereby providing a basis for formulating more equitable and sustainable regional Islamic finance development policies and strategies.

Keywords: Sharia financial Institutions; UMKM ecosystem integration

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1. INTRODUCTION

The development of Islamic financial institutions (IFIs) that are fully integrated with the MSME ecosystem is an important strategic step to strengthen more inclusive economic growth in Indonesia (Beby Kendida Hasibuan, 2024). In the context of North Maluku, this integration is particularly relevant given the regional economic structure dominated by UMKM activities, especially in the trade, fisheries, agriculture, and processing industries. Although UMKM in North Maluku have significant local resource potential, their productivity and competitiveness are still limited by limited technological capabilities, limited access to information, and a lack of financing facilities that suit their needs. This is where the role of Islamic financial institutions becomes very important as an alternative financial system that is more inclusive, ethical, and adaptive to the characteristics of micro and small businesses (Hartanto, Suparyanto, & Azwar, 2023). However, to date, Islamic financial institutions and UMKM in North Maluku have not been optimally managed, as reflected in the lack of integration of policies, assistance mechanisms, and service patterns that are responsive to the needs of business actors.

Challenges related to access to capital, Islamic financial literacy, regulation, institutional capacity, and the lack of an integrated digital ecosystem are major obstacles to expanding the reach and effectiveness of Islamic financial services, especially in supporting sustainable UMKM financial inclusion (Mujiatun and Badawi, 2023). On the other hand, there are also significant opportunities. The high Muslim population, growing interest in Islamic financial products, and the national agenda to strengthen the Islamic economy provide strategic opportunities for Islamic financial institutions (IFIs) in the region to grow faster and contribute to strengthening the local economy, including poverty reduction efforts through productive financing (Fadly et al., 2021). In addition, local MSMEs based on the unique natural and cultural resources of North Maluku have the opportunity to enter broader markets if supported by an appropriate and sustainable sharia financing system.

This context makes it important to examine the challenges and opportunities in developing LKS that are integrated with the UMKM ecosystem in North Maluku. The existence of LKS, such as BSI and BPRS, Cooperatives, and BMT, has not been able to provide comprehensive solutions in line with the needs of UMKM. Many UMKM still rely on informal financing sources with high costs and schemes that do not support the sustainability of their businesses (Hossain et al., 2023). On the other hand, Islamic financial institutions also face internal constraints, such as limited human resources, lack of product innovation, minimal use of sharia fintech, and a developing governance structure (Mubarok et al., 2023).

The research questions posed in this study are how to overcome the challenges and opportunities in developing Islamic financial institutions that can be effectively integrated with the MSME ecosystem in North Maluku, and what integration model can optimize the role of Islamic financial institutions in driving regional economic growth. This research is important because good integration between the Islamic finance sector and UMKM will have a significant impact on strengthening the local economy, equitable welfare, and reducing financial access inequality.

The development of Islamic economics in Indonesia in recent years has shown a positive trend, both in terms of government policy, product innovation by Islamic financial institutions,

and asset growth (Supriadi et al., 2023). However, its contribution at the regional level still varies and is often not in line with local economic potential (Supriadi et al., 2023). In North Maluku, Although there are several active Islamic financial institutions, integration with the MSME ecosystem has not yet reached a systematic and sustainable form (Mochlasin, 2023). In addition, the development of UMKM as the backbone of the North Maluku economy also faces fundamental challenges related to limited access to financing, low financial literacy, minimal managerial skills, and lack of utilization of digital technology in business management (Okfalisa et al., 2022). This situation has resulted in most MSMEs operating on a limited scale and struggling to grow sustainably (Okfalisa et al., 2022).

On the other hand, Islamic financial institutions, which should play a role as strategic partners For UMKM, there are also various internal obstacles, such as limited human resources, a lack of product innovation that is suited to the characteristics of micro businesses, and suboptimal digital infrastructure and regulations in supporting service integration (Hassan & Rabbani, 2022). The mismatch between the needs of UMKM and the capacity of Islamic financial institutions has resulted in significant opportunities for Islamic economic development at the regional level not being optimally utilized (Setiawan et al., 2024). This calls for research that not only describes the problem but also provides a framework for institutional transformation and integrative strategies based on local needs (Kassim et al., 2021). In an effort to address the problems and gaps described above, this study focuses on formulating objectives that can guide the analysis and produce relevant recommendations for the development of Islamic financial institutions in North Maluku.

The objectives of this study are to analyze the main challenges faced by Islamic financial institutions in supporting the UMKM ecosystem in North Maluku, covering aspects of regulation, internal institutional capacity, technology utilization, and the level of literacy of UMKM actors; to identify various strategic opportunities that have the potential to strengthen the integration between Islamic financial institutions and UMKM, including market potential, government policy support, digital technology developments, and opportunities for cross-sector collaboration; and to formulate strategic directions or integration models that can serve as a basis for recommendations for local governments, Islamic financial institutions, and UMKM actors to increase Islamic financial inclusion and promote sustainable regional economic growth. With this focus, this study is expected to contribute both theoretically and practically to efforts to develop a more adaptive, innovative, and contextual Islamic economy in line with regional conditions.

The Concept of UMKM

Micro, Small, and Medium Enterprises (UMKM) are the backbone of the economy in many developing countries, including Indonesia (Lubis & Salsabila, 2024; Sinha et al., 2024). UMKM are characterized by their relatively small scale of operations, limited capital, and simple organizational structure. According to Law Number 20 of 2008 concerning Micro, Small, and Medium Enterprises, the criteria for each UMKM category are determined based on assets and turnover. UMKM play a strategic role in employment, income distribution, and community economic empowerment (Syarif et al., 2025). The role of UMKM is not only limited to their contribution to Gross Domestic Product (GDP) and employment, but also in creating strong economic networks at the local level (Muis, 2025). UMKM are often a source of innovation and adaptation to local market needs. Their widespread presence, even in remote areas, makes UMKM

an important instrument in distributing economic prosperity (Lubis & Salsabila, 2024). However, the challenges faced by UMKM are often related to limited access to adequate financial resources for expansion and improvement of product or service quality (Sinha et al., 2024; Alshater et al., 2023). This problem becomes even more crucial when MSMEs operate in areas with underdeveloped infrastructure (Muis, 2025).

The Concept of Sharia Financial Institutions (LKS)

Sharia Financial Institutions (SFIs) are business entities engaged in finance based on Islamic principles (Wijaya et al., 2023; Tok & Yesuf, 2022). SFIs include various types of institutions, ranging from Islamic banks, Islamic insurance (takaful), Islamic capital markets, to Islamic pawnshops. Islamic banks, as the main entities in the Islamic financial system, operate based on a dual banking system in Indonesia, alongside conventional banks (Sukardi, 2022). The development of Islamic banks in Indonesia continues to show a positive trend. Although their market share is still relatively small, their significant annual growth is an encouraging sign (Rahmawati et al., 2024). LKS plays a crucial role in facilitating financial intermediation in accordance with sharia, channeling funds from surplus units to deficit units, and encouraging inclusive and equitable economic growth (Tok & Yesuf, 2022).

LKS not only functions as a financial intermediary institution, but also as an agent of economic development based on Islamic ethical values (Wijaya et al., 2023). Bank Indonesia (BI) and later the Financial Services Authority (OJK) have established various regulations to ensure that LKS operations are in accordance with sharia principles and able to compete with conventional financial institutions (Asyiqin, 2025). These regulations cover aspects of capital, governance, risk management, and consumer protection. In an effort to encourage the growth of Islamic banks, the strategies developed include encouraging financing for the productive sector, product innovation, coordination with regulators, increasing efficiency through synergy, as well as socialization and education for the community so that understanding and trust in Islamic banks will become stronger (Gustati et al., 2023).

In addition to Islamic banks, there are also non-bank Islamic financial institutions that contribute to the Islamic financial ecosystem, such as Islamic financing companies, Islamic pension funds, and baitul mal wa tamwil (BMT). BMT, in particular, plays an important role in serving MSMEs because of its focus on empowering the people's economy and utilizing social funds (zakat, infaq, sadaqah) (Anwar et al., 2023). The existence of BMTs often serves as a bridge between MSMEs and the more formal financial system, offering microfinance and sharia- compliant savings products that are more accessible to small business owners (Hani et al., 2025).

Integration of Sharia Finance with the UMKM Ecosystem

The integration of LKS with the UMKM ecosystem refers to the interconnection and synergy between various parties in the Islamic economic system, such as Bank Syariah Indonesia (BSI), BPRS, BMT, Islamic cooperatives, the government, UMKM actors, supporting institutions, and digital infrastructure, which together support financing, business assistance, marketing, and capacity building for business actors (Khayuni & Walida, 2025). Various studies on the interrelationship between programs of Islamic financial institutions, government agencies, and UMKM actors show that multi-party partnerships can expand the scope of empowerment efforts,

reduce potential financing risks, and encourage business sustainability (Sukmana et al., 2020). The effectiveness of these partnerships will be even stronger if accompanied by mentoring, training, and institutional strengthening at the local level (Hartanto et al., 2023). A number of studies also show that the application of Islamic financing, such as murabahah, mudharabah, and musyarakah, can encourage the development of UMKM in Indonesia (Hartanto et al., 2023). This positive impact will be even more pronounced if Islamic finance practices are carried out in a supportive policy environment and supported by the use of digital technology (Khayuni & Walida, 2025). The concept of a sharia ecosystem places MSMEs not merely as recipients of financing, but as an integral part of a value network that encompasses financial, legal, social, and da'wah dimensions (Judijanto et al., 2025). This ecosystem approach emphasizes the integration of commercial and social instruments (zakat, infaq, sadaqah, waqf) as the foundation for strengthening UMKM capital and resilience (Judijanto et al., 2025).

Challenges in Developing LKS that are Integrated with the UMKM Ecosystem

The literature identifies a number of key challenges in developing LKS that are truly integrated with the UMKM ecosystem. First, regulatory and policy challenges, such as the fragmentation of MSME support policies, limited incentives for sharia financing, and suboptimal data integration between regulators, LKS, and UMKM support institutions (Saifurrahman & Kassim, 2024; Kartika et al., 2025). Second, internal institutional challenges within LKS, including limited human resources who understand both the characteristics of UMKM and sharia principles, conventional MSME risk analysis capabilities, and slow innovation of products that truly meet the needs of small businesses (Kartika et al., 2025). Third, challenges on the UKM side, namely low Islamic financial literacy, minimal understanding of Islamic contracts, low quality of financial reports, and limited collateral and business track records, which make the financing eligibility assessment process difficult (Suryani & Baidhowi, 2025). Fourth, technological and infrastructure challenges, such as unequal internet access, limited integrated sharia-based information systems, and limited use of digital platforms by sharia UMKM (Devi et al., 2023).

Opportunities for Strengthening LKS–UMKM Integration

On the other hand, various studies also highlight the great opportunities for developing LKS integrated with the UMKM ecosystem. First, the momentum of strengthening national regulations and policies in the sharia finance sector, including the OJK's encouragement to expand sharia financial inclusion and UMKM financing, opens up space for collaborative innovation between LKS, the government regions, and business actors (Harahap et al., 2025). Second, the development of the digital economy and the penetration of technology-based Islamic banking and financial services provide opportunities to expand the reach of services to previously underserved areas, including islands and remote areas (Osman & Elamin, 2023). Third, a number of empirical studies show that Islamic financing designed in accordance with the characteristics of UMKM can drive business growth, improve financial performance, and strengthen long-term sustainability, especially when synergized with mentoring and training programs (Menne et al., 2022; Hartanto et al., 2023). Fourth, the growing public interest in halal products and the Islamic economy has created a large market niche for Islamic-based UMKM, so that the integration of LKS–UMKM is not only a functional financing requirement but also part of a regional economic development strategy with a strong Islamic identity (Batubara & Ritonga, 2024).

2. METHODS

This study uses a qualitative approach with a descriptive design to gain an in-depth understanding of the social, institutional, and economic dynamics related to the integration of Islamic financial institutions (IFIs) and the UMKM ecosystem in North Maluku. The qualitative approach is relevant for analyzing complex and contextual phenomena, as emphasized by Dahal et al. that qualitative research is capable of exploring social meanings in depth through direct interaction with research subjects (Dahal, 2025). A descriptive design is used to map the actual conditions of LKS and MSMEs, including regulatory barriers, internal capacity, service preferences, and opportunities for multi-stakeholder collaboration (Ghoni et al., 2024). The selection of Ternate City as the research location is based on the high concentration of UMKM and LKS activities and the availability of relevant key informants.

Primary research data was obtained through in-depth interviews and field observations, while secondary data was obtained from documentation studies (Nur Izzati Binti Mohamad Anuar et al 2024). Semi-structured interviews were used because this format provides flexibility for researchers in exploring informants' perceptions, in accordance with the qualitative research guidelines described by Weng Marc Lim (Lim, 2025). Informants included LKS leaders (BSI, BPRS, BMT, sharia cooperatives), productive UMKM actors, and sharia economic practitioners. Informants were selected based on the principle of saturation, which is commonly used in qualitative research to determine the saturation point of information (Im et al., 2023). Field observations were conducted to obtain a direct picture of LKS-UMKM service practices and their interactions (Anuar et al., 2024).

Data analysis was conducted through thematic analysis with the stages of transcription, coding open coding, axial coding, and selective coding, as described in the qualitative analysis guidelines by Kyungmee Lee (Lee, 2020). These coding stages enable researchers to identify thematic categories and formulate core themes related to the challenges, opportunities, and strategies for LKS-UMKM integration (Masdah et al., 2025). The use of this analysis technique is also in line with the findings of Syafitri et al., which confirm the effectiveness of the s tepwise coding approach in systematically organizing qualitative data (Masdah et al., 2025). The validity of the findings is maintained through source and technique triangulation, as well as the application of the principles of credibility, transferability, reliability, and confirmability as recommended by Ni Made Dhian Rani Yulianti et al. in modern qualitative research practices (Yulianti & Kintani, 2020). This study also adheres to research ethics, including written consent, informant confidentiality, voluntary participation, and responsible use of data. The documentation study reinforces data triangulation.

3. RESULTS AND DISCUSSION

The research findings show that UMKM in Ternate City develop within an informal economic framework supported by social relationships, direct transactions, and daily business patterns. These practices shape a business orientation that emphasizes family economic sustainability and flexibility in capital and risk management. In this context, the relationship

between UMKM and formal financial institutions, including Islamic financial institutions, is selective and situational.

The interaction between UMKM and Islamic financial institutions shows a mismatch between the normative acceptance of sharia principles and technical readiness in accessing financing services. Business actors tend to understand the basic values of the sharia economy, while the administrative and conceptual aspects of contracts still require a process of adaptation. From an institutional perspective, this condition is understood as part of the structural challenges in bridging the formal financial system with the dynamic and contextual nature of the local economy.

The views of UMKM actors towards Islamic financial institutions reflect a paradox between trust in values and economic prudence. Islamic financial institutions are considered ethical and trustworthy, but are also seen as having consequences that need to be carefully considered in the context of business uncertainty. These findings confirm that the integration of UMKM and Islamic financial institutions is a socio-economic process that requires an adaptive, relational, and understanding-based approach to local economic practices.

Key Challenges in the Integration of Islamic Financial Institutions and UMKM in North Maluku

a. Regulatory and Policy Challenges of the UMKM Ecosystem in LKS-UMKM Integration

Research findings indicate that nationally applicable sharia financing regulations are not yet fully aligned with the business realities of UMKM in island regions such as North Maluku. UMKM business practices in traditional markets and the fisheries sector have developed within an informal economic framework based on family, social, and local trust relationships. In this context, formal legality requirements such as Business Identification Numbers (NIB), business licenses, and written accounting records are often not part of everyday business practices. Sharia financial institution leaders acknowledge that this administrative unpreparedness is a major obstacle in the financing process, even though the businesses are considered viable and sustainable (Sulaiman & Suparman, 2025). From the researchers' perspective, this condition reflects the tension between formal regulatory logic and local economic logic, where financing policies have not fully accommodated business forms that have developed outside the modern administrative system.

In addition to legality issues, this study reveals that Islamic financing risk assessment schemes have not fully accommodated the seasonal and fluctuating nature of UMKM businesses. The fisheries and marine product trade sectors, which are the backbone of the local economy, are greatly influenced by fishing seasons, weather conditions, and product distribution. Cash flows in this sector do not follow a stable and linear income pattern, making them difficult to evaluate using standard risk instruments. The head of BPRS Ternate emphasized that a uniform approach to assessing eligibility often fails to capture the dynamics of fishermen and fish traders (Haly, 2025). This view is reinforced by Islamic economics scholars who argue that the absence of a context-based risk approach makes it difficult to optimally implement profit-sharing agreements (Suparman, 2025). Researchers' interpretations indicate that the risk issue is not merely a technical banking problem, but rather a policy design issue that is not yet sensitive to the seasonal economy characteristic of island regions.

Another notable finding is the lack of regional policies that are explicitly integrated with Islamic economic development. UMKM empowerment programs run by local governments tend to focus on general aspects of entrepreneurship, while integration with Islamic financial institutions remains partial and sectoral. The Head of the North Maluku Province Cooperative and UMKM Office stated that strengthening UMKM requires a synergistic policy framework between institutions so that sharia literacy, bookkeeping assistance, and digitization can be implemented in an integrated manner. (Kusman Malik, 2025). From the researcher's point of view, the absence of an integrated regional policy framework has caused UMKM and LKS development efforts to run separately. Contextually, these findings confirm that the integration of LKS-UKM in North Maluku is not only related to business readiness or the flexibility of financial institutions, but is also largely determined by the alignment of regional policies in building a sharia economic ecosystem that is in line with local social, cultural, and economic characteristics.

b. Internal Capacity Challenges of Islamic Financial Institutions

The results of the study show that the internal capacity of Islamic financial institutions (IFIs) remains a limiting factor in strengthening integration with the UMKM ecosystem in North Maluku. One of the main challenges lies in the nature of Islamic financing products, which are not yet fully adapted to the realities of micro businesses in the archipelago. In practice, financing accessed by MSMEs tends to be centered on murabahah contracts because they are considered simpler and easier to understand, while profit-sharing contracts such as musyarakah and mudharabah are relatively rarely used. LKS leaders acknowledge that the application of profit- sharing contracts requires intensive assistance and the availability of adequate business data, which UMKM often do not have (Malik, 2025). From the researcher's point of view, the dominance of murabahah reflects the internal risk mitigation strategy of LKS, but at the same time shows the limitations of product innovation in responding to the collective, seasonal, and trust-based nature of UMKM businesses.

In addition to product design, the marketing and education approaches of LKS have not fully reached UMKM groups at the grassroots level. Observations and interviews show that outreach activities tend to be conducted through formal forums and limited meetings, thus failing to reach fishing communities, traditional market traders, and UMKM on small islands. Sharia economics academics emphasize that this limited reach has caused sharia literacy to develop unevenly, even though culturally, the community has a high normative acceptance of Islamic economic principles (Syaifuddin, 2025). The views of UMKM actors reinforce this finding, as they assess that access to information about sharia products still depends on individual initiatives to visit bank offices (Saleh & Lukman, 2025). The researchers' interpretation shows that the limitations of the community-based marketing approach create an institutional distance between LKS and UMKM, so that LKS is not yet fully present as part of the local socio-economic ecosystem.

Another internal challenge relates to the limited number of human resources (HR) with cross- disciplinary competencies. LKS HR generally has strong capacity in administration and risk analysis, but assistance for UMKM requires additional skills such as simple bookkeeping, daily cash flow management, and digital literacy. The leaders of BPRS and BSI Ternate emphasized that business assistance often requires time and competencies beyond conventional banking tasks (Harly & Suparman, 2025). From the researchers' perspective, this condition shows a gap between

the operational orientation of LKS as formal financial institutions and the needs of UMKM for educational and relational assistance. Contextually, these findings confirm that strengthening the integration of LKS–UMKM in North Maluku requires not only product innovation but also the transformation of LKS's internal capacity towards an Islamic financial institution model that acts as an empowerment partner, not merely a financing provider (Malik, 2025).

c. Challenges in the Use of Digital Technology

Research findings indicate that the use of digital technology in the integration of Islamic financial institutions (IFIs) and UMKM in North Maluku still faces structural challenges influenced by the geographical conditions of the archipelago. Field observations and interviews reveal an imbalance in access to digital infrastructure between urban areas and surrounding islands. In areas such as Hiri Island, Moti Island, and the coastal region of Tidore, limited internet connectivity means that Islamic digital banking services cannot be accessed consistently. ISI leaders emphasize that these connectivity limitations hinder the equitable implementation of mobile banking and digital payment systems, even though ISIs have prepared adequate digital platforms (Sulaiman & Harly, 2025). From a researcher's perspective, this condition reflects a regionally based digital divide, meaning that the digitalization of Islamic finance is not yet fully inclusive for UMKM in island regions. In addition to infrastructure constraints, this study found that the digital literacy of UMKM remains a significant challenge in utilizing technology-based Islamic financial services. UMKM actors generally manage their businesses with manual records and are not accustomed to using digital financial applications to monitor cash flow or compile business reports. Sharia economics academics assess that these limitations in digital literacy are not only related to technical capabilities, but also to business patterns that have long relied on cash transactions and interpersonal trust (Abbas & Syaifuddin, 2025). UMKM actors themselves reveal that the use of financial applications is often considered complicated and irrelevant to their daily business needs (Lukman, 2025). Researchers' interpretations show that low digital literacy has direct implications for UMKM' ability to meet Islamic financing requirements, as the business data expected by Islamic financial institutions is not available in a structured format.

Another challenge that has arisen relates to the design and features of the LKS digital application, which is not yet fully oriented towards the needs of small UMKM. The interview results show that UMKM need automatic financial recording features, simple financing simulations, and visual or voice assistance to facilitate understanding for traditional market traders. However, the Islamic banking applications currently available still focus on basic transaction functions such as transfers and payments. From the researcher's point of view, this condition shows that the digitization of LKS is still oriented towards the operational efficiency of institutions, not yet fully oriented towards user empowerment. Contextually, these findings emphasize that digital transformation in the integration of LKS–UMKM in North Maluku requires a more adaptive, contextual, and user-experience-oriented approach so that technology does not become a new barrier but rather a tool for inclusive Islamic economic empowerment (Suparman & Malik, 2025).

d. Literacy and Capacity Challenges for UMKM in LKS–UMKM Integration

Research findings show that the Islamic financial literacy of UMKM actors in North Maluku is still at a basic conceptual level, mainly limited to a normative understanding of the prohibition of usury. Observations in traditional markets show that technical terms such as contracts,

murabahah margins, and profit-sharing mechanisms are not yet operational knowledge for business actors. This condition causes some UMKM to view Islamic financial institutions as having no substantial difference from conventional institutions. The Head of the Sharia Compliance Unit at the Ternate Branch of Bank Muamalat emphasized that this misunderstanding often arises because business actors see fixed installments without understanding the underlying contract structure (Sulaiman, 2025). A similar view was expressed by Islamic economics academics who assessed that Sharia literacy at the UMKM level has not yet touched on the functional dimension, so that the principles of justice and partnership in the Islamic economy have not been fully internalized in business practices (Syaifuddin, 2025). Interpretatively, these findings indicate that low Islamic literacy is not only a matter of information, but also related to the absence of contextual and continuous education processes.

In addition to sharia literacy, limited financial recording capacity is a fundamental challenge in integrating UMKM with sharia financial institutions. Field observations show that most business actors still rely on memory or small notes without a standard format in managing daily transactions. This condition makes it difficult for UMKM to present the business data required in the financing assessment process. UMKM actors admit that they are not accustomed to preparing income statements or cash flow statements because their business activities are carried out intuitively and based on experience (Idris & Saleh, 2025). From the perspective of Islamic financial institutions, weak financial recording has a direct impact on the limited application of profit-sharing contracts, which require transparency and clarity of business performance (Harly, 2025). The researchers' interpretation shows that financial record-keeping issues cannot be separated from the characteristics of micro UMKM operating in a subsistence economy, where the main objective of the business is daily survival, not capital accumulation and expansion.

The challenges of literacy and capacity among UMKM are exacerbated by the local economic culture, which still relies on a trust-based lending system. Informal lending practices between traders, delayed payments to suppliers, and dependence on debt collectors, especially in the fisheries sector, are the main mechanisms for meeting business capital needs. This pattern is considered faster, more flexible, and more in line with the daily rhythm of business than formal financing. The Head of the North Maluku Province Cooperative and UMKM Office emphasized that the dominance of the informal economy makes UMKM feel that there is no urgency to interact with formal financial institutions, including LKS (Malik, 2025). From the researcher's point of view, this condition reflects the strength of social capital in the local economy, but at the same time poses structural challenges for LKS-UMKM integration. Contextually, these findings confirm that strengthening sharia literacy and UMKM capacity must be done with an approach that respects the local economic culture, so that LKS can be positioned not as a replacement for existing trust relationships, but as partners that strengthen business sustainability.

Strategic Opportunities for LKS and UMKM Integration in North Maluku

a. Market Potential Based on Local Leading Sectors

Research findings indicate that the economic structure of North Maluku provides natural opportunities for LKS-UMKM integration through local leading sectors that have long been the basis of community livelihoods. The fisheries and maritime trade sectors occupy a central position, with daily and seasonal capital requirements. The business patterns of fishermen and fish traders,

which depend on the fishing season and weather conditions, show conceptual compatibility with sharia contracts such as murabahah for working capital for operational needs, family or group-based musyarakah, and seasonal mudharabah during the sea harvest period. LKS leaders emphasize that this sector is the backbone of the regional economy and has great potential for development through more flexible sharia financing (Akbar Sulaiman, et al., 2025).

In addition, traditional markets such as Gamalama Market and Bastiong Market function as daily economic centers with rapid and repeated capital turnover. Trading activities involving basic necessities, marine products, and daily consumer goods form a socially stable micro ecosystem. In this context, LKS has a strategic opportunity to strengthen sharia-based microfinance based on short-term capital needs. Sharia economics academics assess that traditional markets are not only transaction spaces, but also social spaces rich in trust capital, so they can be an effective entry point for community-based sharia financing (Sofyan Abbas, 2025). Contextually, the growing potential in the culinary and tourism sectors in Ternate City also opens up financing opportunities for product, equipment, and packaging innovations, which are in line with the goal of increasing the added value of local UMKM. Researcher's Interpretation. Opportunities based on local leading sectors show a natural alignment between the economic characteristics of the North Maluku community and the principles of Islamic financing. The challenge of integration does not lie in the absence of a market, but rather in the ability of LKS to design products and approaches that are contextual to the rhythm of local business.

b. Government Policy Support and Regulations for UMKM Development

The results of the study show that the economic structure of North Maluku provides natural opportunities for the integration of LKS-UMKM through local leading sectors that have long been the basis of people's livelihoods. The fisheries and maritime trade sectors occupy a central position, with daily and seasonal capital requirements. The business patterns of fishermen and fish traders, which depend on the fishing season and weather conditions, show conceptual compatibility with sharia contracts such as murabahah for working capital for operational needs, family or group-based musyarakah, and seasonal mudharabah during the sea harvest period. LKS leaders emphasize that this sector is the backbone of the regional economy and has great potential to be developed through more flexible sharia financing (Sulaiman & Harly, 2025).

Capacity building programs such as training in financial record keeping, business legality management, and UMKM digitization have great potential to be synergized with LKS. Academics assess that so far, capacity building and UMKM financing have been carried out partially, so that cross-sector policy integration is key to strengthening the ecosystem (Syaifuddin, 2025). From the perspective of LKS, collaboration with local governments is considered strategic in preparing UMKM to be better equipped to access formal financing (Sulaiman, 2025). Researchers' interpretations indicate that policy support confirms that LKS-UMKM integration is not only a matter for financial institutions, but also part of the regional development agenda regional development agenda. Regulatory synergy has the potential to transform sharia financing from a mere financial instrument into part of an economic empowerment policy.

c. Digital Technology Development as a Driver of Integration

The development of digital technology has emerged as an important opportunity to accelerate the integration of LKS and UMKM. The use of QRIS in traditional markets has begun to function as a gateway for digital transaction recording, especially in the culinary and daily trade sectors. LKS leaders and local governments note that although adoption is not yet widespread, the adoption of QRIS in urban areas such as Ternate and Tidore shows an increasing trend (Sulaiman & Malik, 2025). This opens up opportunities for the transformation of cash transactions towards a more recorded system.

In addition, mobile Islamic banking services are beginning to be accepted by UMKM that have access to smartphones, especially for payment transfers, raw material orders, and balance monitoring. Academics emphasize that if developed contextually, for example through simple Sharia- based financial recording applications, digitization can be a game changer for UMKM readiness to access financing (Abbas & Syaifuddin, 2025). However, these findings also show that the success of digitization is highly dependent on user-friendly application design and direct assistance in the field (Sulaiman et al., 2025). Researchers' interpretations show that digital technology serves as an enabler, not a single solution. Contextual digitization can bridge the administrative gap between UMKM and LKS assessment requirements, while accelerating Islamic financial inclusion.

d. Opportunities for Cross-Sector Collaboration as an Ecosystem Strengthener

The interview results show that opportunities for cross-sector collaboration are one of the main strategic factors in the LKS-UMKM integration model. Potential forms of collaboration include cooperation between LKS and local governments in literacy and administrative assistance, with universities in product design and sharia contract education, and with mosque communities and MSMEs for Islam-based socialization. LKS leaders and academics agree that a collaborative approach is more effective than independent sectoral intervention (Sulaiman et al., 2025).

This cooperation is considered capable of utilizing the social and religious capital of the North Maluku community as a gateway to strengthening the sharia economy. Local governments emphasize that multi-stakeholder synergy can accelerate the process of making UMKM more creditworthy without neglecting the local social context (Malik, 2025). Researchers' interpretations show that cross-sector collaboration represents an ecosystem-based Islamic finance approach, where LKS-UMKM integration is built through a network of complementary actors. Contextually, this model is most relevant for archipelagic regions with community-based economic structures such as North Maluku.

Strategic Direction and Integration Model for Islamic Financial Institutions (LKS) and UMKM in North Maluku

The strategic direction for the integration of Islamic financial institutions (LKS) and UMKM in North Maluku needs to be developed through a multidimensional approach that focuses not only on financing products, but also on strengthening the capacity of business actors and adapting to the socio-economic context of the archipelago. The integration model formulated in this study consists of three interconnected main pillars, namely the empowerment of UKM literacy and administrative capacity, contextual Islamic product innovation, and inclusive digitalization as

a means of expanding Islamic financial services. These three pillars are understood as an integrated ecosystem that works simultaneously, rather than as separate partial interventions.

The first pillar places Sharia literacy and UMKM administrative capacity as the foundation for integration. Research findings show that low administrative readiness and technical understanding of Sharia contracts are initial obstacles that prevent UMKM from interacting effectively with LKS. Therefore, the formulated strategy emphasizes community-based Sharia literacy, such as markets, mosques, and fishing villages that are in line with the social structure of North Maluku society. Simple bookkeeping assistance and UMKM legality clinics are positioned as empowerment tools, not merely as a means to meet financing requirements. The hybrid (offline-online) training model has strong contextual significance because it overcomes the geographical challenges of the archipelago, allowing for the continuous transfer of knowledge despite physical access limitations. According to the researchers' interpretation, this pillar serves as a mechanism for transitioning from the informal economy to a more inclusive formal sharia financial ecosystem.

The second pillar emphasizes the importance of sharia product innovation derived from the characteristics oflocal businesses. Family musyarakah contracts, seasonal mudharabah for the fisheries sector, and short-term daily micro murabahah are efforts to contextualize sharia principles into the realities of community businesses. Character-based lending systems are interpreted as recognition of social capital and community trust, which have long been the foundation of the local economy. From the researcher's perspective, these product innovations show that the principles of justice, partnership, and sustainability in Islamic economics can be flexibly operationalized without losing their sharia integrity. This pillar also confirms the shift in the role of LKS from mere financing providers to business partners who understand the dynamics of the community economy.

The third pillar complements the integration model through inclusive digitalization and the expansion of Islamic financial services. Strategies such as mobile LKS agents, the integration of Sharia QRIS in traditional markets, the development of simple financial recording applications, and business monitoring dashboards are understood as adaptive digital tools. Digitalization in this model is not merely understood as technological efficiency, but as an empowerment tool that helps MSMEs gradually adapt to modern financial systems. Contextually, inclusive digitalization is an important bridge between the informal cash economy and the formal Islamic financial system in the archipelago. Researchers' interpretations emphasize that the effectiveness of this pillar is highly dependent on cross-sector synergies between LKS, local governments, universities, and communities, which together build an Islamic financial ecosystem based on local wisdom.



Figure 1. Image of the LKS–UMKM Integration Model in North Maluku

The LKS–UMKM integration model formulated in this study emphasizes that the success of Islamic financial inclusion in North Maluku is not determined by a single factor, but rather by the interaction between literacy, product innovation, and digitalization that is sensitive to the local context. Theoretically, this model enriches the discourse on Islamic finance with a community-based and context-oriented integration approach. Contextually, this model is relevant as a strategic framework for LKS policies and practices in strengthening the role of UMKM as pillars of the regional economy, while also having the potential to be replicated in other island regions with similar economic characteristics.



Figure 2. Diagram of Contextual Sharia Integration Model Based on Literacy, Assistance, and Inclusive Digitalization.

Inclusive Digitalization illustrates that successful integration between sharia financial institutions (SFIs) and UMKM is not linear or determined by a single factor, but rather the result of the interaction of various mutually reinforcing elements within the ecosystem. Continuous improvement in sharia literacy is the main foundation for UMKM players to adequately understand the principles and mechanisms of sharia finance, which is then strengthened through structured business assistance in managerial, administrative, and legal aspects. This foundation facilitates the

development of Islamic financial products tailored to local business characteristics, so that the principles of fairness, partnership, and sustainability can be applied contextually. Digitalization that is adaptive to the archipelagic conditions serves as a means to expand access and service efficiency, while overcoming the geographical limitations faced by UMKM. This process becomes effective and sustainable when supported by cross-sector synergies between LKS, local governments, universities, and communities, making this model relevant as a basis for formulating policies and strategies to increase sharia financial inclusion in North Maluku.

Implications of Findings for the Development of the Sharia Finance Ecosystem

The results of the study show that the development of the Islamic finance ecosystem in North Maluku cannot be understood solely as a technical issue of financing and regulatory compliance, but rather as a social process that is greatly influenced by cultural interactions, literacy levels, and the digital readiness of the community. The implications of these findings emphasize that Islamic financial institutions need to adopt a culture-based approach in their education and marketing strategies, utilizing social spaces such as markets, fishing communities, and religious institutions so that the message of Islamic finance is more easily accepted and trusted. On the other hand, simplifying procedures and administration is an urgent need to improve UMKM access, but this must be carefully designed so as not to neglect the principles of prudence and sharia compliance. These findings also show the importance of developing seasonal sharia products, especially for the fisheries sector, so that financing schemes are more in line with the local business income cycle. In addition, strengthening multi-stakeholder collaboration between LKS, local governments, universities, and communities is a prerequisite for the implementation of sustainable and contextual business assistance. In this context, inclusive digitalization plays a strategic role as a bridge for the transition from informal economic practices to the formal Islamic financial system, while still considering the limitations of infrastructure and digital literacy in the archipelago.

Overall, the analysis shows that the challenges and opportunities in developing LKS integrated with the UMKM ecosystem in North Maluku reflect the gap between the design of formal financial institutions and the reality of the local economy. The research findings confirm the theoretical basis that the success of Islamic finance is not only determined by contract compliance, but also by institutional adaptability, literacy, and contextual ecosystem integration. Therefore, inclusive and economy-based LKS-UMKM integration in North Maluku requires the transformation of the role of LKS into Islamic financial institutions based on empowerment, collaboration, and local wisdom, as mandated in the principles of Islamic economics and UMKM ecosystem theory.

4. CONCLUSION

Based on the results of this study, it can be concluded that the integration of Islamic financial institutions (LKS) with the UMKM ecosystem in North Maluku is a complex process and is greatly influenced by the socio-economic characteristics of the archipelago. The challenges of integration are not only technical in nature, but also based on the incompatibility between the design of formal financial institutions and informal, seasonal, and social relationship-based

practices of UMKM. The lack of Islamic financial literacy, limited administrative capacity of UMKM, internal readiness of LKS, and uneven use of digital technology are major obstacles to effective integration.

On the other hand, opportunities to strengthen the integration of LKS-UMKM are wide open in line with the dominance of the fisheries sector, traditional trade, and community-based businesses that are in harmony with Islamic finance principles. Government policy support, increased public acceptance of Islamic economics, digital technology developments, and the potential for cross-sector collaboration are strategic assets in building an inclusive and sustainable Islamic finance ecosystem. Based on these findings, this study formulates a contextual sharia integration model that emphasizes synergy between sharia literacy, business assistance, financing product innovation, and inclusive digitalization. This model shows that the success of LKS-UMKM integration is determined by the interaction of a multi-stakeholder ecosystem, thus providing a strong empirical basis for formulating policy recommendations and strategies for further development of regional sharia finance.

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