



Challenges of Implementing Total Quality Management in Addressing the Financing Risks Faced by Islamic Banks

Shafiq Mohammed Al-Dhahabi

¹ Department of Computer Science, College of Basic Education, University of Altoosi, Iraq; e-mail: shafeeq.mohammed@altoosi.edu.iq

Author correspondence: Shafiq Mohammed Al-Dhahabi

Abstract: The radical transformations toward business economies and knowledge-based information have become a focal point for writers and researchers, particularly in the fields of public administration and financial management. These changes have significantly affected the banking industry, especially with the liberalization of global markets for financial and banking organizations, along with the rapid technological advancements and information shifts. Such transformations have inevitably led to alterations in banking performance, with new methods being adopted to address emerging challenges in the banking sector. In this context, Total Quality Management (TQM) has emerged as a crucial concept with a clear impact on banking performance. Its significance is particularly evident within Islamic banks, as they play a vital role in the global banking system, operating under a set of unique principles and practices. The effectiveness of TQM in improving the operational efficiency and risk management strategies of these institutions cannot be overstated, as these banks consistently demonstrate financial sufficiency, often exceeding required ratios. However, despite their financial stability, Islamic banks face challenges in fully implementing the principles of TQM. This study seeks to explore how the requirements of TQM can help reduce financing risks in Islamic banks by enhancing service quality, improving customer satisfaction, and optimizing internal processes. By examining the relationship between TQM practices and risk management strategies, this research aims to offer insights into how Islamic banks can better navigate the complexities of modern financial landscapes while ensuring continued growth and stability. Through this study, the potential for TQM to serve as a strategic tool for reducing financing risks in Islamic banks will be assessed, contributing to a more sustainable and competitive banking environment.

Keywords: Challenges; Financing Risks; Islamic Banks; Quality Management

1. Introduction

1.1 Background

Islamic banking has emerged as one of the indispensable pillars of financial structures in most nations, providing a Sharia-compliant alternative to traditional banking by focusing on ethical investment, risk sharing, and the exclusion of interest-based transactions. The sector has proven resilient and expanding, specifically in the Middle East, North Africa, and Southeast Asia, where market shares and customer bases continue to grow in search of ethical and socially responsible financial services (Andespa et al., 2024; Nugroho, 2021).

Despite this growth, the Islamic banking sector faces multifaceted challenges driven by globalization, financial market liberalization, and rapid technological advancements, including digital banking and the emergence of internet-based financial services. The liberalization of financial and banking services has heightened competition, compelling Islamic banks to enhance operational efficiency while ensuring compliance with Sharia principles (Badwan, 2024).

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In addition, the current technological revolution obliges banks to embrace sophisticated information systems and digital platforms to cope with customer demands for speedier, more efficient, and easy-to-use services. The trend to digitalization calls for Islamic banks to ensure high degrees of quality in operations while handling the risks attached therewith, especially those concerned with financing operations in changing economic and regulatory landscapes (Scott, 2024).

Islamic banks also mostly have trouble in maintaining stable service quality during their operations due to diverse perceptions of compliance with Sharia, diverse requirements of customers, and dynamically changing market conditions. Such complications increase exposure to the financing risks, namely credit risks, liquidity risks, and operating risks, which will undermine their stability and competitiveness unless they are managed proactively (Rozie et al., 2023).

The modern-day complex environment requires Islamic banks to implement Total Quality Management (TQM) to promote service quality, business processes, and risk management methodologies. TQM relies on the principle of constant improvement, customer focus, and full organizational membership participation for the sake of quality promotion in all banking functions (Ikra et al., 2021). By implementing the principles of TQM, Islamic banks would align business practices with customer needs and regulatory pressures to promote competitiveness, customer satisfaction, and risk minimization of financing in the long term (Faizi, 2024). The paper explores how embracing TQM will enable Islamic banking institutions to reduce financing risk whilst ensuring high quality service standards, providing practical recommendations for Islamic banking institutions seeking to embed operational excellence and financial soundness in the face of rising competition and changing financial landscapes.

1.2 Research Problem

The Islamic banking services sector functions in the presence of intricate and continuously changing environmental and competitive pressures, where adaptation is needed on an ongoing basis to ensure stability and development. One of the salient features of the environment is the continuous liberalization of financial and banking services in many nations, including the Arab world, due to the widening of market access and deepened competition in financial institutions. Furthermore, the fast development of the information and technological revolution, as represented in the advent and proliferation of internet banking, has drastically altered the operating environment of banking services (Novikov et al., 2020). The developments have created new customer demands for speed, access, and quality of service, pushing the banks to redefine and improve the operating structures.

Against this backdrop, Islamic banks, guided by the principles of Sharia that stress ethical and interest-free banking, must confront the dilemma of staying competitive in the marketplace while being faithful to the essence of their philosophy. Outdated cost

competition techniques no longer apply in this changing landscape. Islamic banks must increasingly turn to the more modern concepts of competition based on operational excellence and superior quality services and processes (Haron et al., 2020). This shift is important not just for sustaining customer confidence and satisfaction but also for countering the various financing risks, namely the credit risk, the liquidity risk, and the operations risk, by virtue of which the financial soundness and image of Islamic banks might suffer seriously (Jarbou et al., 2024).

To surmount these impediments in an effective manner, Islamic banks must implement contemporary management approaches, and one of the indispensable approaches is Total Quality Management (TQM). TQM stresses the achievement of constant improvements, customer-focused functions, and quality enhancements in organizational operations for which the goals of Islamic banking align reasonably well (Alsoukini et al., 2025). Through the implementation of TQM, Islamic banks can increase the quality of their services, refine internal operations, and bolster risk management practices, hence placing themselves competitively in the banking industry in addition to meeting their moral responsibilities and ensuring long-term survival in a competitive financial landscape.

1.3 Research Significance

It is significant because it adds to the systematic and clear understanding of Total Quality Management (TQM) and the mechanisms for its implementation in the Islamic banking system. Through the study of the practical application of TQM, the study reveals how its principles can increase the procedural operations, ensure constant improvements, and enhance the quality of banking services in compliance with the principles of Sharia. Through one of its key contributions, TQM has the potential to reduce financing risks in the form of credit, liquidity, and functional risks, being significant Islamic banking issues due to the special procedural approaches and the compliance requirement.

In addition to this, the study presents the application of TQM as being central in the appraisal and measurement of the performance of Islamic banks. By embracing the practices of TQM, Islamic banks can effectively assess in a systematic way their sustainability and continuity in operations amidst the ever-changing financial marketplace. This process enables management and other stakeholders to identify areas for improvement, enhance transparency, and implement quality-focused strategies that directly contribute to customer satisfaction and the fulfillment of client expectations.

Additionally, the study underscores the alignment of TQM with the ethical and customer-centric focus of Islamic banking, illustrating how TQM can support Islamic banks in delivering reliable, high-quality services while maintaining financial stability and operational efficiency. By adopting TQM, Islamic banks are better positioned to meet regulatory requirements, strengthen their market position, and contribute to the broader objectives of ethical finance and sustainable banking practices.

1.4 Research Objectives

This study aims to:

- a. Examine the concept and components of Total Quality Management and its fundamental requirements.
- b. Clarify the application and activation of TQM in Islamic banks.
- c. Address the mitigation of financing risks within the performance of Islamic banks.

1.5 Research Hypothesis

The study is based on the following primary hypothesis:

Islamic banks can implement Total Quality Management to reduce financing risks under normal operational conditions, provided that:

- a. There is a competent and aware management team committed to the importance and implementation of TQM.
- b. Employees have a clear understanding of TQM and its role in achieving both organizational and individual objectives.
- c. A supportive legislative environment exists, allowing Islamic banks to apply TQM without causing harm to their surrounding environment.
- d. Sufficient material resources are available to facilitate necessary changes, including replacing outdated machinery with modern equipment, conducting essential training programs for staff development, and introducing modern technologies that can enhance the quality of banking services.

2. Challenges of Total Quality Management in Mitigating Banking Financing Risks

2.1 General Concepts of Total Quality Management

Total Quality Management (TQM) is a recent management technique whose popularity has spread in the last three decades in many industries because it has a broad scope for quality improvement and organizational sophistication. The idea of quality management at first was limited to the quality of tangible products by minimizing defects and complying with standards in the producing processes. TQM, on the other hand, has been widely advanced to involve all organizational processes and services as a general organizational improvement and sustainability framework (Butt & Chamberlain, 2025).

TQM represents a systematic methodology designed to ensure that all planned activities and processes within an organization are executed effectively and consistently. It serves as a preventive approach aimed at avoiding problems before they occur, emphasizing proactive management practices that encourage the efficient utilization of both material and human resources. By focusing on prevention rather than correction, TQM enables organizations to minimize waste, reduce operational errors, and lower costs while maintaining high-quality outputs (Pawanr et al., 2025).

At the core of the philosophy of TQM is the organizational holism in management, in which all departments, functions, and employees collectively strive for ongoing improvement (Lameijer et al., 2023). An important part of TQM is improving the attributes of goods and services important to customers, acknowledging the fact that customer satisfaction determines organizational success to a significant degree. It involves bringing organizational culture, values, assumptions, and operating practices in line to institutionalize quality as part of the collective accountability of all the workers at all hierarchical levels to ensure employees remain committed to quality improvement activities (Rahnuma, 2020).

In the banking services environment, TQM presents important benefits by helping the top management redefine functions, duties, and practices in operations to be in line with quality goals. It inculcates the ethos of constant improvement by bringing employees forward to point out inefficiencies and participate in the perfecting of processes and practices in delivering services. By employing the application of TQM, the banks achieve excellence in the services rendered to the customer by being consistent, dependable, and responsive in operations, the vital ingredients in the competitive banking industry. In the long run, the implementation of TQM in banking achieves higher customer satisfaction due to the emphasis on customer needs accompanied by increased operating efficiency (Testa et al., 2024). Through the implementation of the culture of quality, banks have the potential to enhance marketplace competitiveness, increase stakeholder confidence, and ensure longer-term sustainability. The implementation of TQM hence becomes a strategic resource vital to banking institutions seeking to manage changing conditions in the marketplace and maintain focus on the delivery of high-quality service and customer-orientated practices.

2.2 Objectives of Total Quality Management

The main goals of Total Quality Management (TQM) involve the creation of organizational culture in which ongoing improvement becomes integral to routine operating procedure in such a way that quality enhancement becomes the natural and recurring process throughout the functional areas. TQM puts quality in the foreground at all organizational levels because it acknowledges the fact that all processes and activities, no matter how large they might be, come collectively to determine the quality of end products and services being rendered to the customers (Reza et al., 2025).

The central focus of TQM is the prevention of errors and inefficiencies rather than merely detecting and correcting them after they occur. By adopting preventive measures, organizations can reduce the likelihood of defects, minimize rework, and enhance the reliability of their services and products, which contributes to cost reduction and operational efficiency (Grigg, 2021). This proactive approach not only saves resources but also strengthens customer trust by ensuring consistency and dependability in service delivery.

TQM works to enhance productivity by streamlining processes and waste eradication to help organisations obtain more output with efficient resource utilization. Improved

productivity, accompanied by more quality in the process, contributes to greater profitability, which is vital for the organisation's sustenance and development. Furthermore, by being proactive to quality and customer demands, the TQM allows the organisation to maintain its existing customer base by acquiring additional customers based on favorable word-of-mouth, establishment of the organisation's credibility, and consistent service provision (Pawanr et al., 2025).

Also, TQM instils the sense of individual accountability and ownership by encouraging the active participation of employees in quality improvement activities and process refinement. The sense of organizational belonging makes employees more willing and more motivated to exert efforts in the direction of organizational goals (Permana et al., 2021).

TQM also seeks to increase the quality of services and products at large and at the same time lower business operations costs and reduce time and effort wastages. The balance between cost effectiveness and quality enhancement serves to help organizations deliver value to the customer in return for financial stability (Eze et al., 2020).

TQM achieves its goal of breaking down organizational silos by fostering interdepartmental collaboration and teamwork, where the goal is to achieve shared objectives. The result is effective problem-solving, sharing of the best practices, and collective action for ongoing improvement. Through these processes, TQM assists business organizations in enhancing market share and long-term financial benefits, building competitiveness in increasingly changing and competitive business landscapes (Loving, 2021). With the incorporation of operating practices to customer expectations and focused sustainable quality development, customer satisfaction is maintained by TQM and the survival and long-term success of the enterprise organization is guaranteed.

2.3 Importance of Total Quality Management

The value of Total Quality Management (TQM) is in assisting the organizations in attaining strategic goals like employee involvement, customer satisfaction, and improving the competitiveness to attain sustainability in the environment of fluctuating market competition. By executing quality in the complete organizational system, the TQM assists the organizations in streamlining the processes, minimizing the inefficiencies, and carrying out systematic improvements focused on customer needs and industry standards (Aichouni et al., 2024). (Aichouni et al., 2024).

In banking, the implementation of TQM has the promise to generate significant cost savings by minimizing waste and operating duplication that inevitably stems from the absence of systematic quality management. Through the increase in the effectiveness of processes and the trimming of unnecessary expenditures, banks can use resources more effectively and achieve greater profitability and financial soundness (Ahinful et al., 2025). Through the value placed by TQM on continual quality improvement, banks can provide reliable quality services, which are important to customer satisfaction and loyalty. The satisfied customer becomes

more likely to maintain long-term relationships with his or her bank and provide recommendations for its services, assisting in the broadening of the customer base and the achievement of market competitiveness.

In addition, TQM instils a culture of teamwork, partnership, and trust among employees by promoting active involvement in quality improvement activities and engaging workers in problem-solving and decision-making activities (Ahmed et al., 2025). The participative culture makes workers feel more attached to the organisation and encourages them to play positively to the organisation's goals whilst instilling accountability and ongoing learning. An engaged workforce whose skills and efforts matter are more likely to work effectively, innovate, and maintain high standards of service, all of which lead to the provision of outstanding customer experience.

TQM also encourages the establishment of a productive and healthy organizational workplace by promoting communication, openness, and sharing and exchange of ideas between different organizational departments. The kind of environment, aside from assisting in aligning organizational goals to individual goals, aids in the recognition and repairing of flaws that could impact service quality. Shared commitment and teamwork of the sort greatly assists in helping organizational entities benefit from fostering resilience and agility amidst market developments (Azhar Mohd Harif et al., 2022).

Lastly, the implementation of TQM helps business firms realize competitive advantage by positioning themselves as customer-focused and quality-conscious firms. By high standards of service, efficient operations, and customer-focused orientation, TQM encourages long-term orientation and sustainability, and enables business firms, including banks, to thrive in competitive business environments in realization of strategic objectives.

2.4 Key Requirements of Total Quality Management Adopted in This Study

In this study, the following key requirements of TQM are adopted as independent variables in examining their role in mitigating financing risks in Islamic banking:

2.4.1 Customer Focus

Customer focus is the foundation of Total Quality Management (TQM), and it stresses the point that customers are not just the receivers of the service but part of the service providing process. In TQM, the perception of quality is established by the customer, and therefore, customer feedback becomes critical in terms of providing direction to ongoing improvement initiatives in the organization. In banking, customer focus means actively soliciting, studying, and implementing customer feedback to optimize processes, service quality, and effectively meet the needs of the clients. This way, banking services become customer-focused and aligned with customer expectations, leading to trust and customer satisfaction, as well as the competitive advantage of the bank. By understanding customer needs first, the banks themselves come to know the areas where they lack in terms of service and carry out targeted fixes for the purpose of improving the customer experience over time.

Customer focus in the end builds strong customer relationships, fosters customer loyalty, and sustains business growth by ensuring quality efforts reflect the changing needs and wants of the customer directly (Alsaqer et al., 2024; Lepistö et al., 2024).

2.4.2 Continuous Improvement

Continuous improvement is a fundamental principle of Total Quality Management (TQM), emphasizing that all organizational processes should undergo ongoing evaluation and refinement. This principle focuses on achieving correctness from the outset while maintaining consistent improvement rather than relying on occasional enhancements. In the banking sector, continuous improvement drives efficiency and effectiveness across all services, ensuring that processes remain aligned with evolving customer needs and industry standards. With systematic identification and rectification of inefficiencies, financial institutions reduce the costs of operations, maximize profitability, and maximize service deliveries. The culture of continuous improvement also instills proactive action in financial institutions, encouraging employees to seek innovative solutions and carry out the best practices to refine their performance. With this approach, financial institutions are in a position to continuously deliver high-quality services, reinforce customer satisfaction, and maintain a competitive position in the financial marketplace. Essentially, the culture of continuous improvement supports the long-term survival of financial institutions by instilling adaptability, resilience, and excellence in all operations. (Elmobark et al., 2023).

2.4.3 Leadership

Effective leadership is the key to the successful application of Total Quality Management (TQM) in banks. Leaders play the pivotal role in creating the culture for quality by leading the teams to make ongoing improvements and align organizational objectives with quality objectives. The leadership in TQM entails the fostering of the kind of environment where cohesive teamwork occurs, where collective goals are more important than individuals' interests for the purpose of enhancing the effectiveness of operations. The role of the leaders is to provide for ongoing quality audits, proper documentation, and regular assessments to aid in the provision of quality-focused banking services (Hespe et al., 2022). By providing open communication and fostering the involvement of employees in quality activities, the leaders create a responsible and commitment-oriented culture at all organizational functions. The kind of leadership ensures quality improvement becomes the essence of the operations of the bank, ensuring ongoing service excellence, customer satisfaction, and long-term financial industry competitiveness whilst remaining aligned to the philosophy of ongoing improvement and customer orientation.

2.4.4 Employee Involvement

Employee involvement is a key component of Total Quality Management (TQM), focusing on empowering staff through appropriate training and the delegation of authority to enable them to perform their roles effectively (Casteleiro & Mendes, 2022). By enabling

employees with the right skills and knowledge, financial institutions empower employees to feel confident and participate in quality improvement exercises. By instilling individual accountability and participation in exercises in solving problems, employees feel responsible and part of ownership, prompting them to participate actively in delivering quality objectives. Not only is individual and organizational effectiveness enhanced by promoting the culture of ongoing improvement and collaboration, but the culture of teamwork and ongoing development allows employees to feel more willing to identify inefficiencies and propose sensible solutions, enhancing service quality and customer satisfaction. Employee participation indirectly aids in the sustainable application of TQM in financial institutions, aligning staff activities with quality criteria and organizational objectives (Bashar et al., 2024).

2.4.5 Training and Education in TQM Practices

It is vital to train employees in Total Quality Management principles and practices for the effective implementation of quality programs in banking institutions. Employee training develops the skills and knowledge of employees to impact service quality positively and improve customer interactions. Through the comprehension of practices in TQM, employees feel more ready to identify areas of quality improvements and contribute to quality enhancement activities directly (Waqanimaravu & Arasanmi, 2020). Continuous training also supports the organization in maintaining high-quality standards, ensuring that employees remain updated with best practices and evolving customer expectations. This ongoing development fosters a culture of continuous improvement and accountability, reinforcing employee contributions toward achieving organizational goals. Additionally, regular training initiatives promote confidence among employees, encouraging them to take initiative in quality-related activities and to collaborate effectively with colleagues. Through structured training programs, banks can strengthen their commitment to quality, improve service delivery, and maintain competitiveness in the market while aligning operational practices with customer needs and quality objectives (Walters Glombik, 2020).

3. Financing Risks In Islamic Banks

Islamic banks operate based on real investment and specific types of trade contracts within an environment that exposes them to various risks, some inherent to their operations and others stemming from external factors. These risks directly or indirectly impact profitability, investment value, and the bank's ability to meet its obligations.

3.1 Concept of Islamic Banks

Islamic banking is a contemporary model that, despite being only a few decades old, has secured a position in both the general and Islamic banking markets due to its distinct operational principles and objectives.

Definition: An Islamic bank is a financial institution that fully complies with Islamic Sharia in all its activities, including the prohibition of interest, avoidance of excessive uncertainty, adherence to lawful practices, and commitment to zakat obligations.

3.2 Sources of Funds in Islamic Banks

a. Internal Funds:

- 1) Paid-up Capital: Funds actually paid by the bank's owners.
- 2) Reserves: Amounts deducted from net profits for the bank's sustainability.
- 3) Retained Earnings: Portions of profits withheld before distribution to shareholders.
- 4) Provisions: Amounts set aside to cover potential losses.

b. External Funds:

Islamic banks also require external funds to support their activities, including:

- 1) Demand Deposits: Like conventional banking, these deposits can be withdrawn at any time, although Islamic banks typically place less emphasis on them.
- 2) Non-demand Deposits: These involve profit-sharing investment accounts with depositors under Sharia-compliant contracts, including:
 - a) Savings Deposits: Withdrawable at any time while aiming to grow depositor income.
 - b) Investment Deposits: Long-term deposits with returns based on investment outcomes, including general investment accounts (participating in overall bank results) and specific investment accounts (allocated to specific projects with profits shared and losses borne by the depositor).

3.3 Activities of Islamic Banks

Islamic banks engage in:

a. Investment Activities:

- 1) Direct Investment: Banks directly manage specific projects.
- 2) Financing: Providing funds in return for profit-sharing (e.g., mudarabah, musharakah) or fixed returns through contracts such as murabaha and istisna.

b. Service Provision:

- 1) Banking Services: Fee-based services provided without interest.
- 2) Social Services: Including interest-free loans (qard hasan), zakat distribution, and mutual assistance initiatives.

3.4 Types of Financing Risks in Islamic Banks

Islamic banks face several financing risks, including:

3.4.1 Risks in Profit-and-Loss Sharing (Musharakah)

Musharakah involves the bank participating as a full or partial partner in a project, sharing profits and losses according to predetermined ratios. While it aligns with Sharia principles, this mode involves significant risks, including:

- a. Funding Source Risks: Islamic banks primarily rely on short-term deposits, limiting the feasibility of long-term projects and constraining the bank's ability to select the most profitable ventures.
- b. Investment Diversification Risks: Limited diversification across projects and sectors can increase exposure to sector-specific downturns.
- c. Human Resource Risks: The bank's ability to manage risks depends heavily on the skills and experience of its staff in identifying, evaluating, and monitoring projects.
- d. Project-related Risks: Related to the legal form, growth stage, size, and viability of the project.
- e. Management Risks: Dependence on the competency, integrity, and commitment of the project's management team.
- f. Market Risks: Related to the nature of the product, technological dependence, the presence of substitutes, and competition levels.
- g. Financing Method Risks: Linked to the financial position and commitment of the partner, the size of the financing, and the duration of the partnership.

3.4.2 Risks in Mudarabah Financing

Mudarabah involves profit-sharing where the bank provides capital and the entrepreneur manages the business, sharing profits according to an agreed ratio while losses are borne by the capital provider. Risks include:

- a. Profit Distribution Challenges: Misestimating effort and returns can expose the bank's capital to losses.
- b. Asset Damage Risks: Loss of goods due to unforeseen circumstances, with the bank bearing the financial loss.
- c. Delay in Settlement: Prolonged settlement by the entrepreneur can immobilize the bank's funds and increase opportunity costs.

3.4.3 Risks in Murabaha Financing

Murabaha, especially the "Murabaha to Purchase Orderer" model, is widely used for its perceived simplicity and lower risk profile. However, it carries risks such as:

- a. Default Risk: Client payment defaults can immobilize funds, and legal recourse may be lengthy and costly.
- b. Fixed Profit Margin: The bank's profit remains fixed regardless of payment delays, unlike conventional banks, which adjust interest rates or impose penalties.
- c. Asset Ownership Risks: The bank bears the risk of asset damage or legal obstacles in transferring ownership during the transaction process.

3.4.4 Risks in Ijarah Financing

Ijarah involves leasing assets with the bank retaining ownership while clients use the assets for a fee, with options for the client to eventually own the asset in some cases. Risks include:

- a. Market Risks: If the leased assets are not in demand, the bank may face capital immobilization.
- b. Payment Irregularity Risks: Irregular rental payments disrupt cash flow and investment cycles.
- c. Technological Obsolescence Risks: Rapid technological advancements may render leased assets obsolete, exposing the bank to financial loss.

3.4.5 Risks in Istisna Financing

Istisna involves the bank commissioning the manufacture of goods for a client, who agrees to purchase them upon completion. Risks include:

- a. Specification Risks: Goods not meeting agreed specifications can lead to rejection by the client, resulting in financial loss for the bank.
- b. Delivery Delays: Late delivery can allow the client to cancel the contract, leaving the bank with unwanted inventory.
- c. Payment Irregularity: Delays in client payments disrupt the bank's cash flow and reinvestment plans.

3.5 Total Quality Management Evaluations For Mitigating Financing Risks In Islamic Banks

The existence of risks in Islamic banks is inevitable, as banks cannot earn returns without being prepared to bear potential losses. Here, Total Quality Management (TQM) plays a critical role in mitigating the negative impacts of these risks through several mechanisms:

- a. Promotion of Diversification Policies: TQM encourages Islamic banks to adopt diversification across various operational aspects, including geographical coverage, engagement with multiple economic sectors, utilization of diverse financing instruments, and broadening the customer base. This diversification reduces concentration risk and enhances the bank's ability to absorb shocks from specific sectors or markets.
- b. Culture of Risk Management: TQM helps in propounding a culture of risk management in Islamic banks by instilling in all stakeholders the value of risk management for the sustainability of the bank. Efficient risk management in the framework of TQM entails the building of a sound risk information system, the setting up of the units for special legal risk management, and the establishment of technical risk management departments.
- c. Creation of Sufficient Provisions: Implementation of TQM practices mandate the establishment of sufficient provisions to manage prospective risks by assigning due proportions of profits to enhance the financial situation of the bank. It is pertinent to identify the portion of profits assigned to the bank and the one belonging to depositors to maintain equity and clear understanding of risk-sharing.

- d. Collaterals and Guarantee Utilization: Islamic banks utilize collaterals and guarantees by the employing of the principles of TQM to secure funds. However, due to some limitations of Sharia, utilization is limited to sporadic cases. Thus, the banks must carefully discriminate in selecting collaterals by value and liquidity potential in securing the recoverability and safety of funds in the event of default.
- e. Application of Takaful (Islamic Insurance): The takaful is used as risk management, even though debates about its Islamic legality in some cases persist. TQM welcomes the application of takaful to mitigate the risk of banks to unexpected losses in line with the concept of the cooperative risk-sharing principle.
- f. International Regulations Compliance: In implementing TQM, Islamic banks must be compliant with international regulatory standards, including the Basel II guidelines. Islamic banks are not prevented from achieving international supervisory standards, enhancing their resilience and capacity for risk management.

Islamic banks are exposed to different risks and utilize several tools to reduce them but face difficulty in implementing international regulatory standards like Basel I and Basel II. By incorporating the principles of TQM, Islamic banks can integrate effective risk management practices with their operating practices more effectively, ensuring financial soundness, safeguarding stakeholder interests, and improving their competitive position in the fluctuating financial landscape.

4. Conclusions and Recommendations

4.1 Conclusions

Investments in Islamic banks face various risks, including those related to investor clients, investment capabilities, and the operational systems and methods themselves. Due to the unique nature of Islamic banking operations, the risks faced by investments in Islamic banks differ significantly from those encountered by conventional banking institutions. The lack of necessary capabilities and requirements has led to a higher level of risks faced by Islamic financial and banking institutions.

The elevated risk levels within Islamic financial institutions have resulted in numerous negative impacts on the trajectory of Islamic investment activities. The implementation of Total Quality Management (TQM) in Islamic banks supports the establishment of independent, specialized risk management departments reporting to the board of directors. Risk management activities under TQM are subject to effective and independent auditing within Islamic banks, enhancing the effectiveness of risk management processes.

Islamic banks are exposed to financial risks, which can impose additional burdens on shareholders, affecting their profitability while the banks remain obligated to provide returns to depositors, potentially exposing them to reputational risks.

4.2 Recommendations

To improve and strengthen the current state of capital adequacy in Islamic banks in line with sound practices, the following steps are recommended:

Central banks should provide greater attention to Islamic banks, considering their specific characteristics and operational models. Risk management strategies should be developed in alignment with the evolution of banking operations and risk levels through the application of Total Quality Management. Human resources should be enhanced and trained to supervise various risks, developing their capabilities in risk management effectively.

Tools and systems for risk measurement should be developed according to internal assessment methods to maximize their benefits. Efforts among Islamic banks should be unified to adhere to the Islamic Financial Services Board (IFSB) standards in a manner consistent with TQM principles. Collaboration should be fostered to establish specialized rating and evaluation institutions for Islamic banks. Islamic banks should improve the disclosure of their overall risk management strategies in a manner that enables investors and relevant stakeholders to assess the banks' effectiveness in managing risks.

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