ISLAMIC BANKING DEVELOPMENT, MONETARY POLICY, AND ECONOMIC GROWTH: A PANEL MODERATED REGRESSION APPROACH FOR SELECTED ISLAMIC COUNTRIES

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Abstract

This study aims to analyze the influence of Islamic banking developments and monetary indicators on economic growth in nine Muslim-majority countries, with inflation as a variable This study uses a quantitative method with Moderated Regression Analysis (MRA) estimation panel data using secondary data sourced from SESRIC and the World Bank for the 2013–2023 period. Total Assets (TA) has a significant positive effect on economic growth, while Total Funding and Equity (TFE) and Broad Money (BM) have a significant negative effect. The variables of Sukuk Holdings (SUK), Exchange Rate (ER), and inflation do not show a direct influence on GDP. The moderation results show that inflation acts as a quasi-moderator in the TA and TFE variables, but does not become a moderator in BM, SUK, and ER. These findings confirm that price stability is an important prerequisite for the transmission of monetary policy and the intermediation function of Islamic banking to contribute optimally to the real economy. This research contributes novelty by including inflation as a moderation variable in the context of cross-border Islamic finance, as well as providing practical implications for monetary authorities to strengthen macro stability in the development of the Islamic finance industry.

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Keywords: Islamic Banking, Monetary Policy, Inflation, Economic Growth

INTRODUCTION

The application of sharia principles in the operational activities of Islamic banks contributes significantly to the financial stability of the institution. Unlike conventional banks, Islamic banks run their business following Islamic provisions that reject interest (riba), ambiguity (gharar), and speculative practices (maysir). These principles are a unique foundation that influences risk management strategies, liquidity control, and efforts to maintain the financial resilience of Islamic banks (Haikal et al., 2024).

Islamic finance has experienced an acceleration in global growth in recent years. The assets of the global Islamic finance industry are growing significantly and in 2023 reached nearly USD 4.9 trillion growth, indicating that Islamic instruments (banking and capital markets including sukuk) are becoming an important source of financing in many regions. This makes research on the role of Islamic banking on economic growth even more relevant (Niche, 2024).

At the country level, the development of Islamic banking is very diverse but generally shows an expansion trend. Indonesia, as the largest Islamic banking market in Southeast Asia, continues to report an increase in operational indicators and Islamic banking assets (OJK December 2024 statistics), which is relevant to test the contribution of Islamic bank assets to national GDP (Finance, 2024). Pakistan showed a substantial surge in Islamic banking assets, signaling strong penetration in the domestic banking sector so it is reasonable to examine its impact on economic growth (Pakistan, 2024). Turkey (Participtions Banks) also recorded an increase in the market share of Islamic banking assets, indicating that the Islamic banking model is making an increasingly visible contribution to the banking structures of Muslim-majority countries (Rating, 2024).

The phenomenon of inflation in Muslim countries shows fluctuating movements from year to year. Inflation is often triggered by a combination of domestic and global factors, including changes in exchange rates, increased prices of imported goods, and domestic production cost pressures. These inflation fluctuations create economic uncertainty for business actors and the public, because the continuous price increases reduce purchasing power and increase the burden on household consumption. Volatile inflationary conditions also have an impact on productivity, where business actors have become more cautious in expansion and investment (Harahap et al., 2023).

In many academic studies, economic growth in Muslim-majority countries shows a significant correlation with the development of Islamic finance. Previous research has found that countries that implement an Islamic financial system — compared to those that only use a conventional system — can experience higher economic growth (Firdaus et al., 2024). Meanwhile, according to Naz & Gulzar, (2020), Islamic banking assets, sharia financing, and sukuk have a long-term positive relationship with real GDP in many Muslim countries. Bustami & Maulidina, (2025) states that Islamic economic principles can promote sustainable growth in developing Muslim countries, as they focus on productive investment and equitable distribution. However, economic growth in Islamic countries is not always homogeneous. Qoyum & Ihsan, (2023) shows that macro factors such as the political system also have a moderation role in the impact of economic variables on growth in Islamic countries.

Irawan, (2025) states that in an Islamic perspective, monetary policy should not only regulate the supply of money, but must also pay attention to moral and social aspects so that

income distribution is more equitable and economic stability is achieved. Meanwhile, Yovita Sari, (2024) revealed that Islamic monetary policy has great potential in controlling inflation through controlling the money supply and increasing people's purchasing power continuously. On the other hand, comparative studies by Rusanti et al., (2020) shows that Islamic monetary instruments such as the Islamic interbank money market can be used together with conventional instruments in controlling price stability, without sacrificing Islamic values.

Based on previous literature related to the role of Islamic banking and monetary policy, there is a research gap where the research results are inconsistent so that the researcher re-examines the role of Islamic banks and monetary policy in the face of economic growth with inflation as a moderation in Muslim countries. This study offers an empirical contribution by: (1) examining the role of Islamic banking in countries with different levels of Islamic banking development, (2) examining the mechanism of inflation variables as moderation and (3) examining the role of monetary policy on economic growth.

REVIEW OF LITERATURE

Islamic Bangking and Economic Growth

Finance Growth Nexus Theory submitted by Levine & King, (2016) emphasized that the development of the financial sector has an important role in encouraging economic growth through increased mobilization and allocation of funds, efficiency of interchange, and ease of access to financing for the real sector. In the context of this study, the theory explains the relationship between the variables of the Islamic banking sector and economic growth (GDP). The total assets of Islamic banking reflect the capacity of intermediation and the ability of Islamic banks to channel funds for productive activities, so that the larger the assets owned, the stronger their contribution to increasing national output. Total funding, liabilities and equity describe the ability to raise funds from the public and investors, which, in theory, can increase the flow of financing to the real sector and encourage economic growth. Meanwhile, sukuk holdings reflect investment-based financing instruments that can support long-term development, infrastructure, and productive projects that support economic growth. Thus, according to *Finance Growth Nexus Theory*, the growing development of Islamic financial activities both in terms of assets, fundraising, and investment instruments can make a real contribution to accelerating economic growth in Muslim countries (Levine & King, 2016).

Study by Kismawadi, (2023) shows that there is a causal one-way relationship between the development of Islamic finance and economic growth in terms of dynamic causality between variables. This empirical evidence supports the view of financial growth or the supply-led view, which implies that Islamic banks can be considered a key sector that is important in channeling and transferring financial resources between surplus and deficit units in the economies of Saudi Arabia, the United Arab Emirates, Kuwait, Malaysia, Qatar, Bahrain, and Bangladesh.

Research by M. Anwar et al., (2020) shows a significant relationship, both in the short and long term, between the number of offices and deposits of Islamic banks and economic growth. These findings provide evidence of a two-way relationship between the development of Islamic banking and economic growth. Although its market share is still smaller than that

of conventional banks, the results of the study prove that Islamic banking is a rapidly growing sector and is able to make a real contribution to economic growth.

Research results by Ullah et al., (2021) shows the cointegration relationship between Islamic banking financing (IBD) and economic growth (EG) in Pakistan. Positive (negative) shocks in IBD have a significant positive (negative) relationship to economic growth in the long run; However, in the short term, only positive shocks have been proven to have a significant effect on economic growth. These findings show that the relationship between IBD and economic growth is asymmetrical or non-linear in the long term, while it is symmetrical or linear in the short term.

Research by Supriani et al., (2021) stated that in the long term, Islamic bank financing reflected in the positive Financing to Deposit Ratio (FDR) value has a significant effect on increasing economic growth. This finding confirms that Islamic banks have played an important role in encouraging Indonesia's economic growth through the distribution of financing to customers, especially business actors. However, in the short term, the contribution of Indonesian Islamic banks to economic growth has not been significant. This can be caused by the relatively small market share of the Islamic banking industry.

Monetary Policy and Economic growth

Monetary Transmission Mechanism Theory Explain how monetary policy affects the economy through various channels such as interest rates, exchange rates, asset prices, and expectations (Mishkin, 2007). In the context of this study, broad money describes the money supply which is one of the important instruments in the mechanism of monetary transmission. When central banks increase the money supply, liquidity in the financial markets increases, lowering the cost of funding for the real sector, which ultimately encourages increased production activity and economic growth. Meanwhile, Exchange rate is a monetary transmission channel that affects the price of imported goods, export competitiveness, and capital flows. Exchange rate appreciation can reduce import prices but has the potential to weaken export competitiveness, so its impact on economic growth can vary. Furthermore, inflation as a moderation variable plays an important role in strengthening or weakening the influence of these monetary variables on economic growth. When inflation is high, the effectiveness of monetary expansion can be reduced as rising prices suppress purchasing power and reduce real investment. On the other hand, in conditions of stable inflation, changes in the money supply and exchange rates are more effective in stimulating economic activity in accordance with the monetary policy transmission mechanism (Warjiyo, 2006).

In the context of economic growth, monetary policy plays an important role as a key instrument for maintaining macroeconomic stability and encouraging real sector expansion. Through regulating the money supply, interest rates, and exchange rates, central banks can influence the level of investment, consumption, as well as funding costs in the economy. The effectiveness of monetary policy in driving growth is highly dependent on price stability, economic actors' expectations, and the response of the financial sector in channeling liquidity to productive sectors (Chugunov et al., 2021).

Research by Zia & Jamil, (2025) It shows that in the long run the exchange rate has a positive and large influence on economic growth, while inflation and real interest rates have a negative but relatively small impact. The study also found a strong long-term relationship between these variables. Therefore, to achieve sustainable economic growth, the research

findings recommend that policymakers prioritize controlling inflation at low levels as well as encouraging increased investment through more competitive interest rate setting.

Previous studies have found that a continuous increase in the money supply can trigger inflation in the long run, according to the framework Quantity Theory of Money which confirms that the growth of the money supply will have an effect on the price level when other variables are considered constant. However, in the short term, the increase in the money supply has not directly caused significant inflation. These findings are in line with the pattern of monetary policy transmission in several countries, where the influence of policy on prices requires a time lag before the impact on the real economy is seen. In addition, research shows that in China and Vietnam, the correlation between money supply growth and inflation reaching 99.1% illustrates a very strong relationship (Doan Van, 2019).

This research offers novelty by focusing an analysis on the role of Islamic banks and monetary policy in influencing the economic growth of Islamic countries, which has rarely been explored in depth in previous literature. Unlike previous studies that only assessed the direct relationship between Islamic and monetary bank variables and economic growth, this study included moderation variables to see how the mechanism of monetary transmission works more comprehensively. This approach provides a new understanding of the effectiveness of Islamic banking and monetary instruments in the economic context of Islamic countries, while providing empirical evidence that can be the basis for more targeted policymaking.

RESEARCH METHOD

This study uses a quantitative method with estimates *Moderated Regression Analysis* (MRA) panel data (Sekaran & Bougie, 2016) with the aim of finding out whether the main relationship becomes stronger or weaker when the moderation variable is included in the model. The selection of OLS was carried out because this method is able to produce efficient and unbiased estimates as long as the linear regression assumptions are met. The panel data estimation process was carried out using Eviews software, accompanied by classical assumption tests such as heteroscedasticity and multicollinearity to ensure the validity of the resulting model. The data used is sourced from secondary data obtained through SESRIC and the World Bank, in the form of panel data for the period 2013–2023. Purposive sampling technique is used to determine the sample based on the criteria (Martono et al., 2010): (1) Muslim-majority countries or have a growing Islamic banking sector (2) Have complete and available data for all research variables. Based on these criteria, 9 countries: Bangladesh, Indonesia, Jordan, Kuwait, Nigeria, Oman, Pakistan, Turkey, and the United Arab Emirates were obtained as research samples.

Table 1.
Definition of Variable

Variable Types	Variable Name	Unit	Source
Dependent.	Economic Growth (GDP)	USD	World Bank
Independent	Islamic Banking, Total Assets (TA)	USD	SESRIC

	Islamic Banking, Total Funding/Liabilities and Equity (TFE)	USD	SESRIC
	Islamic Banking, Sukuk Holdings (SUK)	USD	SESRIC
	Broad Money (BM)	%	World Bank
	Exchange Rate (ER)	LCU per USD	World Bank
Moderation	Inflation (INF)	%	World Bank

Based on the definition of the variables in Table 1, the regression equation is as follows:

$$\mathbf{GDP_{it} = \alpha + \beta 1TA_{it} + \beta 2TFE_{it} + \beta 3SUK_{it} + \beta 4BM_{it} + \beta 5ER_{it} + \gamma 1(TA_{it} \times INF_{it}) + \gamma 2(TFE_{it} \times INF_{it}) + \gamma 3(SUK_{it} \times INF_{it}) + \gamma 4(BM_{it} \times INF_{it}) + \gamma 5(ER_{it} \times INF_{it}) + \mu i + \lambda t + \varepsilon it}$$

Information:
i = country
t = year
μi\mu_i μi = individual effect (FE/RE)
εit\varepsilon_{it}εit = error term

To choose the most appropriate estimation method, this study evaluated three approaches, namely Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). The results of the Chow Test comparing CEM and FEM showed a p-value of 0.000 (< 0.1), so FEM was judged more accurately. Furthermore, the Hausman Test which tested the difference between FEM and REM also produced a p-value of 0.000, which again confirmed that FEM was the best choice. Thus, this study establishes the Fixed Effect Model as the main estimation method. The use of FEM is considered the most relevant because it is able to overcome potential bias due to neglected variables and is effective for panel data that has fixed characteristics in each unit (country), where the main differences arise between entities rather than all the time.

RESULTS AND DISCUSSION

Classic Assumption Test

The normality test was carried out to determine whether the data in this study followed the normal distribution. Based on the results of processing using the Histogram–Normality Test in Eviews, a probability value of 0.1148 was obtained. Because the probability value is greater than the significance level of 0.05, the data is declared to be normally distributed. This shows that the residual model meets the assumption of normality and is suitable for use in subsequent analysis.

The multicollinearity test aims to find out whether the regression model has a correlation between its independent variables. The results of the multicollinearity test showed that all variables had a correlation value below 0.80 after the SUK variable was transposed.

Thus, there is no indication of multicollinearity, and all variables are declared to pass the test and are suitable for use in regression models.

This study uses the glycer test as a heteroscedasticity test tool. Based on the test results, it was obtained that the probability value of each independent variable was greater than 0.05. Thus, it can be concluded that there is no heteroscedasticity problem in the model and is feasible for further testing.

Table 2.
Multiple Estimation Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.	Conclusion
C	22.50294	0.420703	53.48891	0.0000	Significant
TA	1.558033	0.195764	7.958725	0.0000	Significant
TFE	-1.182884	0.169832	-6.965027	0.0000	Significant
D(SUK)	-0.001788	0.029884	-0.059839	0.9524	Insignificant
BM	-0.008248	0.001661	-4.966839	0.0000	Significant
ER	1.69E-05	3.84E-05	0.438653	0.6622	Insignificant
INF	-0.001032	0.001485	-0.695011	0.4892	Insignificant
R-squared	0.991046				
Adjusted R-squared	0.989375				
F-statistic	592.9396				
Prob(F-statistic)	0.000000				

Source: processed with Eviews 12.

The regression results show that *Total Assets* (FY) has a positive and significant effect on economic growth, where every 1% increase in TA increases GDP by around 1.56%. Instead, Total Funding and Equity (TFE) has a significant negative influence, with an estimate that a 1% increase in TFE actually lowers GDP by around 1.18%, which indicates that the increase in funds or capital has not been used efficiently in encouraging economic activity. *Broad Money* (BM) also showed a significant negative influence, where a 1% increase in the money supply lowered GDP by around 0.008%, describing less effective monetary transmission or monetary pressure that was not optimally absorbed by the real sector. Meanwhile, Sukuk Holdings (SUK), Exchange Rate (ER), and Inflation (INF) have no significant influence on economic growth.

The regression model shows excellent performance, characterized by an R-squared value of 0.9910, which means that 99.10% of the variation of the dependent variables can be explained by the independent variables in the model. The Adjusted R-squared value of 0.9894 also indicates that the results remain strong despite considering the number of variables used. In addition, the value Prob(F-statistic) = 0.0000 indicates that the model as a whole is statistically significant, so that the variables used are able to explain their effect on the

dependent variables simultaneously. The MSE Root value of 0.095 and the S.E. of regression of 0.104 indicate that the model error is relatively small.

Moderated Regression Analysis (MRA)

Total Asset Islamic Banking And Inflation

Table 3.
TA*INF

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	24.33577	0.362850	67.06840	0.0000
TA	0.204502	0.038926	5.253664	0.0000
INF	-0.063895	0.026645	-2.398010	0.0186
TA*INF	0.005926	0.002451	2.418161	0.0177

Source: processed with Eviews 12

The estimated results show that Total Assets (TA) has a positive coefficient of 0.2045 with a probability of 0.0000, so every 1% increase in TA will increase GDP by around 0.204%. However, inflation (INF) actually has a negative and significant effect with a coefficient of -0.0638 (p = 0.0186), which means that a 1% increase in inflation can reduce GDP by 0.064%. The value of the TA*INF interaction coefficient was positive and significant (p = 0.0177). This suggests that inflation acts as a moderation that strengthens the influence of the TA on dependent variables. This means that the higher the inflation, the greater the positive influence of the fiscal year on economic growth, so that inflation in this model acts as a quasi-moderator

Total Funding & Equity Islamic Banking And Inflation

Table 4.
TFE*INF

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	25.17383	0.296878	84.79533	0.0000
TFE	0.121926	0.033615	3.627142	0.0005
INF	-0.049078	0.027707	-1.771327	0.0800
TFE*INF	0.004682	0.002567	1.823741	0.0716

Source: processed with Eviews 12

The moderation results showed that inflation (INF) acted as a quasi-moderator at a significance level of 10 percent. This can be seen from the direct influence of INF on GDP, which is significant (p = 0.0800), as well as the interaction between TFE and INF (TFE*INF), which is also significant (p = 0.0716). Thus, inflation not only affects the performance of Islamic banking directly, but also strengthens the relationship between Total Funding and Equity (TFE) and GDP.

Sukuk Holding Islamic Banking And Inflation

Table 5.
SUK*INF

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	26.17943	0.027916	937.7866	0.0000
SUK	0.014006	0.072026	0.194461	0.8463
INF	0.004408	0.002589	1.702769	0.0926

SUK*INF	-0.002859	0.006185	-0.462276	0.6452

Source: processed with Eviews 12

The moderation results show that inflation (INF) has a direct effect on economic growth at a significance level of 10%, but does not strengthen or weaken the relationship between Sukuk Holdings (SUK) and economic growth, because the interaction variable of SUK*INF is not significant. Thus, inflation does not act as a moderation variable, but only as an independent variable that stands (Predictor of Moderation) on its own without affecting the relationship between changes in sukuk ownership and economic growth.

Broad Money and Inflation

Table 6.
BM*INF

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	26.64036	0.152147	175.0960	0.0000
BM	-0.007860	0.002536	-3.099437	0.0026
INF	0.011506	0.011597	0.992159	0.3239
BM*INF	-0.000173	0.000216	-0.802564	0.4244

Source: processed with Eviews 12

The moderation results showed that *Broad Money* (BM) had a significant effect on economic growth, while inflation (INF) and BM*INF interaction were not significant. This means that inflation does not strengthen or weaken *the influence of Broad Money* on economic growth. With these conditions, this model is included in the category *of homologizer moderation.*

Exchange Rate and Inflation

Table 7.
ER*INF

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	26.64036	0.152147	175.0960	0.0000
ER	-0.007860	0.002536	-3.099437	0.0026
INF	0.011506	0.011597	0.992159	0.3239
ER*INF	-0.000173	0.000216	-0.802564	0.4244

Source: processed with Eviews 12

The estimated results show that the *Exchange Rate* (ER) variable has a significant effect on economic growth at a significance level of 10 percent, while inflation (INF) and the ER*INF interaction are not significant. This shows that inflation is not able to strengthen or weaken the influence of exchange rates on economic growth. Therefore, this model is categorized as a moderation homologizer.

Discussion

The results of the study show that Total Assets (TA) has a positive and significant influence on economic growth in the sample country. Each increase in Islamic banking assets reflects an increase in the ability of Islamic financial institutions to distribute financing to the real sector through sharia-based instruments such as mudharabah, musharakah, or

murabahah. This supports the view *Finance–Growth Nexus Theory* that the greater the capacity for financial intermediation the greater the support for increasing national economic output. Thus, the development of Islamic bank assets makes a real contribution in driving investment, production, and expansion of economic activities in Muslim countries (Chiad & Gherbi, 2024; Farah et al., 2025).

The results of the estimate show that Total Funding/Liabilities and Equity (TFE) has a negative and significant effect on economic growth. These findings indicate that an increase in bank funding sources such as third-party funds and capital is not necessarily followed by the effectiveness of disbursement of funds to the productive sector. This condition can occur if the growth of funds is only deposited as passive assets, absorbed for internal liquidity needs, or has not been optimized in the form of productive financing. In other words, although the ability to raise funds has increased, the effectiveness of its distribution has not been able to encourage optimal economic growth in Islamic countries. This is in line with research that states that the disbursement of funds (credit side), which comes from bank funding, does not necessarily drive growth (Marsuki et al., 2022). Funds are deposited for internal liquidity needs (reflected in liquidity ratios and capital adequacy) or because of poor asset quality (NPLs) that hinder the distribution of productive funds (Amali et al., 2022).

The Sukuk Holdings variable did not show a significant influence on economic growth. This indicates that the increase in sukuk ownership or issuance has not had a direct impact on accelerating economic activity in the study countries. This condition is possible because the placement of sukuk funds is often used for long-term financing whose effects are not immediately visible in the same period, according to Echchabi et al., (2018) because the sukuk market in a number of Muslim countries is still relatively small, so its contribution to GDP is still limited. Thus, sukuk has not yet become an instrument capable of driving significant economic growth in the short term.

Broad Money has a negative and significant effect on economic growth. These findings show that the increase in the money supply in the sample countries actually suppresses economic growth, which can be caused by the transmission of ineffective monetary policies or inflationary conditions that make liquidity not optimally absorbed into the real sector. This condition is in line with the view that money supply growth without an increase in productivity can trigger price pressures and reduce people's purchasing power, thereby weakening economic activity (Jayadi, 2024). Study by Nurfarkhana & Anita, (2021) indicates that after the money supply measured by M2/GDP reach the threshold (*Threshold*) in particular, its effect on economic growth becomes negative because excess liquidity is no longer channeled to the productive sector, but creates *bubble* or price pressures (inflation).

The exchange rate variable has no significant effect on economic growth in the model. This shows that exchange rate fluctuations in the sample country have not been the main determining factor for economic growth in the observation period. This insignificance can occur if the economies of these countries are not yet heavily dependent on foreign currency-based export-imports, or the monetary policy implemented has succeeded in reducing exchange rate volatility so that the impact on growth is not too strong (Laurent et al., 2007).

The results show that inflation acts as a quasi-moderator in the relationship between Total Assets (TA) and economic growth. This is reflected in the significance of the moderation variables and the interaction of TA*INF in the model, which means that inflation not only affects economic growth directly but also strengthens the positive relationship

between Islamic banking assets and GDP. When inflation increases, the contribution of bank assets to economic activity increases, indicating that Islamic banks are able to maintain their intermediation function effectively under price pressures. Thus, the larger the assets managed by Islamic banks, the stronger the impact on economic growth, especially in conditions of increasing inflation. This is explained as found by Maulidiyah et al., (2023) that the focus of Islamic banking is on the real sector that encourages energy consumption.

In the Total Funding and Equity (TFE) variable, inflation again functions as a quasi-moderator because both inflation and TFE*INF interaction are equally significant. These findings show that inflation has a direct influence on economic growth, while moderating the relationship between Islamic bank funding and GDP. The positive interaction coefficient illustrates that the increase in price pressures actually strengthens the funding and capital ability of Islamic banking in encouraging economic activity. This condition can occur when high inflation is responded to by increased demand for financing in the real sector, so that the funding structure of Islamic banks becomes more productive and contributes more to GDP (Khotimah, 2022).

In the Sukuk Holdings (SUK) variable, inflation is not able to moderate the relationship between sukuk and economic growth, because the interaction of SUK*INF is not significant. Although inflation shows its own influence, changes in price levels do not affect the strong or weak contribution of sukuk to GDP. This condition can be caused by the character of sukuk as a term financing instrument Squirt (Pratama et al., 2025), so the impact is not immediately visible in short-term economic fluctuations. In addition, in some countries the sukuk market sample is still relatively small, so changes in inflation are not strong enough to change their effect on national economic performance.

Inflation does not play a moderator role in the relationship between Broad Money (BM) and economic growth, because the BM*INF interaction variable is not significant. Thus, the influence of BM on GDP occurs directly without being influenced by inflationary conditions. This is in line with findings that indicate that the increase in the money supply has not been effectively transmitted to the real sector in both high and low times of high inflation (Warjiyo, 2006). This condition can occur if the monetary transmission mechanism in selected Islamic countries is still not optimal.

The results of the study also showed that inflation did not moderate the exchange rate (ER) relationship with economic growth, characterized by the insignificance of the ER*INF interaction variable. Although the exchange rate shows a direct influence at a 10% significance rate, changes in inflation do not strengthen or weaken the relationship. This illustrates that exchange rate dynamics may be more influenced by external factors such as world commodity price movements, export-imports, or international financial market conditions (Zorzi et al., 2007), so that domestic inflationary pressures do not play a sufficient role in influencing exchange rate transmission to economic performance.

CONCLUSION

This study found that Islamic banking has a very significant influence on economic growth in Muslim-majority countries. Based on the results of the study, governments and monetary authorities in Muslim countries need to strengthen price stability as a prerequisite for the effectiveness of Islamic financial transmission to the real economy. The central bank also needs to ensure that the growth of Islamic banks' assets and funding actually flows

towards the productive sector, not just increasing liquidity without impacting output. In addition, the development of sukuk instruments and the deepening of the Islamic financial market are important to increase their contribution to economic growth.

This study has several limitations. First, the scope of the research country is limited to nine Muslim-majority countries so that the results cannot be generalized to all countries with an Islamic financial system. Second, the methods used have not distinguished the short-term and long-term effects more deeply on each individual country.

For further research, it is recommended to add other variables such as regulatory quality, policy effectiveness index, or indicators of Islamic financial stability so that the results obtained become more comprehensive. Subsequent research may also use the dynamic panel or VAR method to more clearly distinguish short- and long-term effects. In addition, researchers can further expand the research object to more countries or conduct comparative studies between groups of countries to see the differences in the transmission structure of Islamic finance to economic growth

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