



Research Article

The Impact of Regulations on Risk Management Practices in Islamic Financial Institutions Using a Systematic Literature Review (SLR) Approach

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Abstract. The rapid growth of the Islamic finance industry in Indonesia requires the implementation of effective risk management in line with the principles of prudence and sharia compliance. This study aims to systematically identify and synthesize the impact of regulations, both prudential regulations from the Financial Services Authority (OJK) and sharia regulations from the National Sharia Council (DSN-MUI), on risk management practices in Islamic Financial Institutions (LKS). The method used is a Systematic Literature Review (SLR) by searching 219 articles from various international and national academic databases, then selecting 34 relevant articles for in-depth analysis. The results of the review show that regulations have a significant influence in shaping the structure, culture, and effectiveness of risk management in LKS. OJK regulations serve as an external framework that encourages the implementation of Enterprise Risk Management (ERM) to manage eight main types of risk, while DSN-MUI regulations ensure the integration of Sharia Compliance Risk in every financing activity. The synergy between regulations and risk management has been proven to increase financial stability, reduce the Non-Performing Financing (NPF) ratio, and strengthen institutional legitimacy through an increase in Return on Assets (ROA) and Return on Equity (ROE). This study confirms that regulations are not merely a formal compliance instrument, but a strategic foundation for the sustainability and competitive advantage of Islamic financial institutions.

Keywords: DSN-MUI; OJK; Regulations; Risk Management; Sharia Financial Institutions.

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1. Introduction

The global Islamic finance sector has transformed from a niche market segment into one of the main pillars of the world's financial architecture. In Indonesia, this development is a manifestation of the high level of public awareness and demand for financial products based on Sharia principles, which fundamentally reject the practice of riba and emphasize aspects of distributive justice (maslahah) and risk sharing (Arta, 2024).

The growth of this industry is not only quantitative but also strategic. Based on contextual data, by the end of 2022, the total assets of Indonesian Sharia Finance (excluding sharia stocks) had reached IDR 2,375.81 trillion, showing consistent average growth that exceeded the national economic growth rate (OJK in Mas'ut, 2023). This rapid growth, driven by the consolidation of large Islamic banks (e.g., the merger of Bank Syariah Indonesia/BSI), places Islamic Financial Institutions in a crucial position in maintaining financial system stability (Aqlima Geubrina et al., 2025).

Therefore, if high asset growth is not balanced with an adequate internal control framework, the potential for losses due to systemic risk will increase sharply. This stability can only be guaranteed through the implementation of strict and effective Risk Management (Nastiti & Cupian, 2024).

Risk Management in Sharia Financial Institutions is a much more complex issue than in conventional institutions. Sharia Financial Institutions are not only exposed to eight types of general risks (credit/financing, liquidity, market, operational, strategic, reputation, and legal) as regulated by the authorities (Rif et al., 2023), but also face a unique risk, namely Sharia Compliance Risk (Puspa Yanti & Iqbal Fasa, 2024).

This Sharia Compliance Risk has fatal legal and reputational implications. Weaknesses in legal aspects, such as the non-fulfillment of valid contract requirements or weaknesses in agreements, can trigger litigation lawsuits and mass withdrawals (bank runs), which can lead to bankruptcy (Suharto, 2022). The existence of this dual risk is an absolute justification for the need for intervention and guidance from regulators. Empirically, various literature studies have concluded that strong risk management practices—especially in managing Non-Performing Financing/NPF—are significantly positively correlated with the financial performance of Sharia Financial Institutions, as reflected in the increase in Return on Assets (ROA) and Return on Equity (ROE) (Fauzi & Maghfiroh, 2025).

In response, the Financial Services Authority (OJK) has issued a series of imperative regulations, specifically Financial Services Authority Regulation (POJK) Number 65/POJK.03/2016 concerning the Implementation of Risk Management for Sharia Commercial Banks and Sharia Business Units (OJK, 2016). This regulation requires Sharia Financial Institutions to apply prudential principles and an integrated risk management framework, which involves supervision by the Board of Commissioners, the Board of Directors, and, uniquely, the Sharia Supervisory Board (DPS) (Anggraini & Sadewa, 2024).

Although the regulatory framework is solid, the Islamic Financial Institutions industry continues to evolve rapidly, creating an adaptation gap between static regulations and increasingly dynamic business practices. There are two main challenges: (1) The Impact of Digitalization and Product Innovation: The transformation to the digital era has encouraged Sharia Financial Institutions to adopt new products such as hybrid contract-based financing and integration with FinTech to serve MSMEs (Wahyudi, 2024). These innovations pose much more complex operational and information technology risks and have the potential to “outsmart” the traditional risk management framework established by regulators. Sharia Financial Institutions are also required to shift from a partial risk management model to Enterprise Risk Management (ERM) that is fully integrated with sharia principles (Mas’ut, 2023). (2) Effectiveness of Regulation Implementation: On the other hand, the OJK has also proactively issued regulations aimed at preventing abusive lending practices (Nisa Aprilia & Dhian Novita, 2025). The question is, how effective have all these regulations (from POJK Risk Management to DSN-MUI Fatwa and Consumer Protection regulations) been in influencing, changing, and improving the quality of Sharia Financial Institution Risk Management practices in the field?

Previous studies tend to focus on the causal relationship between Risk Management and the performance of Islamic Financial Institutions (Ayu Wandhini, 2024) or judicial analysis of a particular type of regulation (Rahmawati et al., 2024). However, a Systematic Literature Review (SLR) that comprehensively maps, critiques, and synthesizes the collective impact of regulations (as independent variables) on risk management practices (as dependent variables) in the context of Indonesian Islamic Financial Institutions in the modern era is still limited.

Therefore, this research is very important and urgent. Using the SLR approach, this study aims to provide a structured academic synthesis of how the regulatory framework established by the authorities has shaped the responses and risk management practices of Islamic Financial Institutions, so as to provide more accurate policy recommendations for regulators and more adaptive mitigation strategies for practitioners.

2. Literature Review

Regulation

Regulations play a fundamental and imperative role as a key pillar in ensuring the growth, stability, and sustainability of Sharia Financial Institutions (Arta, 2024). In Indonesia, the Financial Services Authority/Otoritas Jasa Keuangan (OJK) is an independent institution that has full control in regulating, supervising, and protecting the financial services sector Rohmah, 2025). This regulatory role is twofold: it provides a legal

basis for the business practices of Islamic Financial Institutions while also directing compliance with prudential principles.

The main regulatory framework governing Risk Management for Sharia Financial Institutions is Financial Services Authority Regulation/Peraturan Otoritas Jasa Keuangan (POJK) Number 65/POJK.03/2016 concerning the Implementation of Risk Management for Sharia Commercial Banks and Sharia Business Units (OJK, 2016 in Anggraini & Sadewa, 2024). This regulation requires Islamic Financial Institutions to implement a comprehensive Risk Management framework to mitigate eight types of common banking risks ((Rif et al., 2023).

However, Islamic Financial Institution regulations have a unique dimension: Sharia compliance. Sharia Financial Institutions must comply with the Fatwa issued by the National Sharia Council of the Indonesian Ulema Council/Dewan Syariah Nasional - Majelis Ulama Indonesia (DSN-MUI), and this compliance is monitored internally by the Sharia Supervisory Board/Dewan Pengawas Syariah (DPS) (Rahmawati et al., 2024). Regulatory failure in this aspect will trigger Sharia Compliance Risk, which can lead to litigation and bankruptcy (Suharto, 2022).

In the contemporary era, regulations continue to evolve adaptively to market dynamics. OJK regulations now also focus on protecting customers from exploitative practices such as abusive lending (Nisa Aprilia & Dhian Novita, 2025) and anticipating the negative impacts of digital innovation, including the emergence of illegal Fintech (Martinus Ahmad et al., 2023). However, regulatory challenges, particularly those related to complexity and inconsistency, remain crucial issues that must be addressed to maximize the potential of Sharia Financial Institutions (A. , & L. N. F. Mahendra Putera, 2024).

Risk Management

Risk Management is defined as a series of processes that include identifying, measuring, monitoring, and controlling risks inherent in all business activities of Sharia Financial Institutions (W. Hajar, 2023). The implementation of effective Risk Management is key to maintaining operational stability, maintaining bank health, and achieving maximum profitability (Nastiti & Cupian, 2024).

The complexity of risk management in Islamic Financial Institutions lies in two main categories of risk:

General Risk: This includes credit/financing, market, liquidity, operational, strategic, reputational, and legal risks (Rif et al., 2023). Financing risk, for example, is a major risk that must be mitigated by Islamic Financial Institutions because it is closely related to the risk of default on products such as murabahah (Melinda, 2023).

Sharia Compliance Risk: This is a risk specific to Sharia Financial Institutions that arises from the failure to comply with Sharia principles in every business activity (Puspa Yanti & Iqbal Fasa, 2024). This risk is crucial because weak legal aspects, such as the non-fulfillment of valid contract requirements, can invalidate transactions and trigger legal risks.

In line with regulatory requirements (POJK 65/2016) and industry developments, the Sharia Financial Institution Risk Management model is moving towards a more integrated approach, known as Enterprise Risk Management (ERM) (Mas'ut, 2023). ERM aims to provide a holistic view of risk, where Sharia risks are integrated into the overall corporate risk management framework (Fauzi & Maghfiroh, 2025). The application of this model is particularly relevant for managing complex innovative products, such as hybrid contract-based financing that has emerged as a result of digitalization (Wahyudi, 2024).

Impact

The implementation of strong and integrated regulations and risk management has a significant impact, both directly and indirectly, on the performance and stability of Sharia Financial Institutions. This impact can be measured through financial performance indicators (KPIs) that reflect the quality of risk management in Sharia Financial Institutions.

In general, the literature shows a strong positive relationship between effective risk management practices and the financial performance of Islamic Financial Institutions. A systematic review proves that good risk management, particularly in operational and liquidity risk mitigation, can improve performance as measured by Return on Assets (ROA) and Return on Equity (ROE) (NOOR et al., 2020).

This positive impact reflects the success of Islamic Financial Institutions in managing their assets and capital efficiently, which in turn improves bank soundness (Nastiti & Cupian, 2024). The most visible impact in the context of Islamic banking is the ability of Risk Management to overcome Non-Performing Financing (NPF).

The disciplined application of Risk Management, starting from the stage of customer risk identification to the collateral binding process, is the main preventive measure to reduce the NPF ratio (Sudanto, 2024). Low NPF is a direct indication of strong credit/financing risk management, which is statistically proven to have a significant effect on the financial performance of Islamic Financial Institutions (Ayu Wandhini, 2024).

Therefore, it can be concluded that regulations act as a trigger and compel Islamic Financial Institutions to adopt Risk Management. Meanwhile, Risk Management functions as an internal mechanism that ensures the adaptation of Islamic Financial Institutions to market dynamics and unique risks (especially Sharia risks), which collectively result in financial stability and improved sustainable performance (Aqlima Geubrina et al., 2025a).

3. Methods

This research is a literature study using the Systematic Review (SR) method, commonly referred to as Systematic Literature Review (SLR), which is a systematic technique for collecting, critically testing, integrating, and compiling the results of various research studies on a research question or topic to be explored (Sugiyono, 2013). The research began with finding articles related to the research topic that would later be studied.

A systematic review is a method of reviewing a particular issue by identifying, evaluating, and selecting specific issues and asking questions that are clearly resolved based on predetermined criteria. This follows previous research that is of good quality and relevant to the research question (Yusuf, 2017).

This study uses the Systematic Literature Review (SLR) method, a systematic, explicit, and reproducible method for identifying, evaluating, and synthesizing research works and thoughts that have been carried out by researchers and practitioners with the aim of recognizing, reviewing, and evaluating all research determined in this study (Chamidi et al., 2025), consisting of several stages, including:

Article Search

The number of articles collected in this study was approximately 219, as shown in Table 2. The articles were obtained from a number of publishers from various reputable international journals, international journals, and national journals. The article search was conducted using the Scopus, Google Scholar, Emerald, Elsevier, and other publisher websites.

However, from the existing number of articles, the titles, abstracts, and full texts were screened to ensure that the articles were relevant to the research topic. The screening process is presented in Figure 1 below.

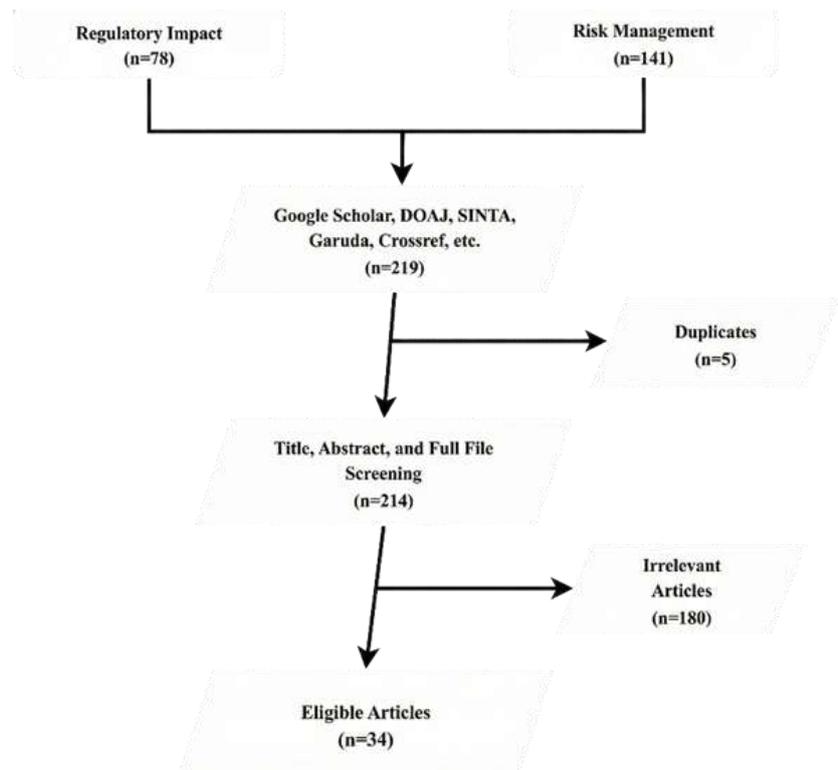


Figure 1. Screening Title, Abstract, and Full Text for eligible data.

Based on the above screening results, 34 articles were deemed suitable to proceed to the systematic review process. The results of the article screening were then mapped based on publisher groups to ensure the distribution of articles in various reputable journals with their respective quartile qualifications. This was done to obtain objectivity and quality of articles that have been discussed in various reputable international journals, as presented in Table 3 below.

Grouping and Determination of Criteria

Furthermore, the articles obtained from the search engine results were then sorted and grouped based on the objectives to be achieved in the study, namely the Impact of Regulation on Risk Management Practices in Islamic Financial Institutions with a Systematic Literature Review (SLR) Approach, then refined in the article review, as illustrated in the flowchart in Figure 2 below (Chamidi et al., 2025).



Figure 2. Flowchart of Systematic Review Articles

Reporting and Presentation

Reporting and presenting the results of a systematic literature review is an interpretation of the literature review study. This report is a summary of the systematic review to provide a clear and detailed picture of what is known in the literature on a topic or research question. This report forms the basis for conducting a database analysis of the articles used. Next, filter and compare the complementary results of the systematic literature review (Massaro et al., 2016).

4. Findings

Based on the data presented in Table 2, information was obtained that articles on the Impact of Regulation and Risk Management were published from 2019 to 2025.

Table 1. Search Results and Number of Articles Collected.

Database Application	Keywords	Number of Articles
Google Scholar, Emerald, Elsevier, dan penerbit lainnya	Impact of Regulator	78
	Risk Management	141
	Number of Articles	219

Source: Processed data, 2025

Table 2. Article Screening Based on Publisher.

No	Publisher	Article
1	Enrichment: Journal of Management	3
2	Asian Journal of Accounting and Governance	2
3	JICN: Jurnal Intelek dan Cendekiawan Nusantara	2
4	JIM (Journal of Islamic Management)	1
5	IJAAF: Indonesian Journal of Applied Accounting and Finance	1
6	Jurnal Hukum Sasana	1
7	JEMBA: Jurnal Ilmiah Ekonomi Manajemen Bisnis dan Akuntansi	1
8	Economics And Business Management Journal (EBMJ)	1
9	Jurnal Penelitian Nusantara	1
10	ADZ DZAHAB: Jurnal Ekonomi dan Bisnis Islam	1
11	Media Hukum Indonesia (MHI)	1
12	Hospitality	1
13	LABATILA: Jurnal Ilmu Ekonomi Islam	1
14	Jurnal Ilmiah Wahana Pendidikan	1
15	INNOVATIVE: Journal Of Social Science Research	1
16	Publikasi Riset Mahasiswa Manajemen	1
17	Jurnal Masalah-Masalah Hukum	1
18	Jurnal Ilmiah Ekonomi Islam	1
19	Maro: Jurnal Ekonomi Syariah dan Bisnis	1
20	Indonesian Journal of Humanities and Social Sciences	1
21	Moderasi : Journal of Islamic Studies	1
22	NISBAH: Jurnal Perbankan Syariah	1
23	MONEY: Journal of Financial and Islamic Banking	1
24	Li Falah: jurnal Studi Ekonomi dan Bisnis Islam	1
25	Asian Economic and Financial Review	1
26	Journal of Accounting and Investment	1
27	Journal of Asian Finance Economics and Business	1
28	Ijtihad: Jurnal Hukum dan Ekonomi Islam	1
29	Al-Manāhij: Jurnal Kajian Hukum Islam	1
30	WADIAH: Jurnal Perbankan Syariah	1
	Number of Articles	34

Source: Processed data, 2025

There are 34 articles analyzed in this article. Content analysis is based on two categories, namely: 1) Regulatory Impact, 2) Risk Management. Keywords are developed from the perspective of the categories to be analyzed in relation to the Impact of Regulation on Risk Management Practices in Islamic Financial Institutions, as presented in Table 4 below.

Table 3. Categories and Keywords of Articles on the Impact of Regulation on Risk Management Practices in Islamic Financial Institutions.

Category	Keywords	Author	Number of Articles
Regulatory Impact	Regulations	(Aprilia et al., 2025; Aqlima Geubrina et al., 2025b; A. Arta et al., 2024; Handayani & Abubakar, 2022; Hidayatullah & Hidayati, 2022; Martinus Ahmad et al., 2023b; Mohd Noor et al., 2020; Rahmawati et al., 2024a; U. Rohmah et al., 2025; Suharto, 2022b)	10
	DSN-MUI Fatwa	(Hidayati & Hidayatullah, 2021)	1
	Shariah Governance	(Alam et al., 2019; Masruki et al., 2020)	2
Risk Management	Shariah Banking	(Hamizar et al., 2024; A. Mahendra Putera & Laily Nisa, 2024; A. Nafik et al., 2025; Wafi et al., 2024; Wahyudi, 2024b)	5
	Risk Management	(Anggraini & Sadewa, 2024b; Ayu Wandhini & Melia Kusuma, 2024; Fasa, 2018; Fauzi & Maghfiroh, 2025; S. Hajar & Wirman, 2023; Hasyim M et al., 2022; Ihyak et al., 2023; Mas'ut et al., 2023; Melinda & Segaf, 2023; Noory et al., 2021; Sudanto, 2024b; Sulistyowati et al., 2023; Syadali et al., 2023; Yanti & Iqbal, 2024)	14
	Risk profile	(Darma & Afandi, 2021; Nastiti & Cupian, 2024a)	2

Source: Processed data, 2025

5. Discussion

Regulations: Not Just Compliance, But the Foundation of Excellence

The Financial Services Authority (OJK) through POJK Number 65/POJK.03/2016 concerning the Implementation of Risk Management requires LKS to manage eight types of risks, such as Credit/Financing Risk, Liquidity Risk, Operational Risk, and others (OJK, 2016). This obligation is a form of affirmation that LKS, as financial intermediary entities, are not immune to market and operational turmoil faced by conventional banks.

This OJK regulation is a formal trigger for LKS to adopt the Enterprise Risk Management (ERM) approach. ERM views risk holistically across all lines of the organization. Without this regulation, MR practices tend to be fragmented, but with the POJK, LKS are forced to measure, monitor, and control risk in a structured manner, which ultimately determines the health of the bank.

Regulations on LKS cannot be simplified as mere formalities, but rather are a foundation that strengthens legitimacy and creates unique competitive advantages in the financial market. This argument is based on two layers of compliance that LKS must fulfill:

First, Prudential Regulatory Compliance (OJK), which requires the implementation of comprehensive Risk Management (RM) as stipulated in POJK 65/2016. This obligation fundamentally forces LKS to adopt prudential standards equivalent to those of conventional banks (Anggraini & Sadewa, 2024).

Second, more crucially, is Sharia Compliance. The regulatory layer from the National Sharia Council (DSN-MUI) and supervision by the Sharia Supervisory Board (DPS) provide a dimension of risk that conventional banks do not have (Rahmawati et al., 2024). Failure at this level will trigger Sharia Compliance Risk, which directly implies Legal Risk (Suharto, 2022). Therefore, Sharia regulations are not only ethical, but also the weakest link that, if broken, can lead to lawsuits and even bankruptcy, which is far more fatal than mere administrative penalties.

In addition, the dynamics of regulations that are adaptive to contemporary issues, such as the prevention of abusive lending (Nisa Aprilia & Dhian Novita, 2025) and anticipation of illegal Fintech (Martinus Ahmad et al., 2023), prove that regulations are a living instrument that continues to move to protect the ecosystem and customers, making them the key to the sustainability of LKS.

Risk Management: A Critical Adaptation Mechanism in Complexity

Risk Management (RM) in LKS has transformed from a mere mitigation function to a critical adaptation mechanism that bridges regulatory demands with the operational realities of business. NPF management cannot be done solely through post-default collection. RM must be applied preventively (Three Pillars of Risk Management): 1) Identification and Measurement: Using qualitative and quantitative analysis (e.g., 5C analysis) at the pre-financing stage to assess customer eligibility and repayment ability (Nafik, 2025; Sudanto, 2024). 2) Control: Through improving the quality of contracts, securing adequate collateral to mitigate Legal Risk, and formulating a loss reserve policy. 3) Reporting System: Fast and accurate reporting enables top management to make timely mitigation decisions.

Low NPF effectiveness is a direct reflection of disciplined and rigorous RM practices.

Institutionally mature LKSs implement an Integrative Sharia and ERM model. There has been a paradigm shift towards integrated Enterprise Risk Management (ERM) (Mas'ut, 2023; Fauzi & Maghfiroh, 2025). MR is no longer sufficient to deal with the eight types of risk separately, but must integrate them into a holistic framework. This integration is urgent given the complexity of current LKS products, especially with the emergence of hybrid contracts and digital transformation (Wahyudi, 2024). ERM becomes the main filter that ensures product innovation remains Sharia-compliant (Compliance Risk) while also being operationally and financially efficient (Operational Risk).

Financing Risk is not only assessed from the perspective of customer economic viability, but also from the validity of the contract used (e.g., murabahah, mudharabah, musyarakah) (Nafik, 2025). If the contract is weak or does not comply with fatwas, then Sharia Compliance Risk arises, which then increases Legal Risk, and if litigation or negative publicity occurs, it will trigger Reputational Risk. MR integration ensures that every

business decision is based on a double risk calculation: financial risk and Sharia validity risk.

In practice, the main focus of MR is on Financing Risk (Credit), which is manifested through efforts to prevent Non-Performing Financing (NPF) (Sudanto, 2024). This analysis confirms that every stage in the financing process from customer character identification to collateral binding is a direct manifestation of a disciplined MR strategy (Melinda, 2023). MR failure in the early stages will result in NPF in the final stages, which de facto becomes a systemic failure of the MR chain mandated by regulations.

Impact: Measurable Stability and Legitimacy

The impact of the synergy between strong regulation and effective Risk Management produces measurable and holistic outputs: Financial Stability, Performance Improvement, and Institutional Legitimacy. Asset Optimization: A decrease in NPF (the result of good Financing MR) directly improves asset quality and reduces financing loss costs. Profitability: Effective Operational and Liquidity Risk Control improves operational efficiency (e.g., through a lower BOPO ratio) and ensures the availability of funds for profitable investments. This is reflected in an increase in the Return on Assets (ROA) and Return on Equity (ROE) ratios. MR turns potential losses into profit stability

Quantitatively, the literature consistently shows that effective MR implementation has a significant positive impact on key performance indicators such as Return on Assets (ROA) and Return on Equity (ROE) (Fauzi & Maghfiroh, 2025; Noory et al., 2021). This relationship is causal: banks that are able to control risk (especially operational and liquidity risk) will have lower operating costs and better asset quality, which directly increases profitability. In addition, the decline in the NPF ratio is the most tangible empirical evidence of the success of credit/financing MR, which in turn reflects a stable level of bank soundness (Ayu Wandhini, 2024; Nastiti & Cupian, 2024).

In the long term, the greatest impact of MR is on the trust capital of Islamic financial institutions. In the Islamic financial market, customers are not only looking for profits, but also blessings and certainty that their funds are managed in accordance with Islamic principles. Critical Argument: Islamic financial institutions that consistently demonstrate sound financial performance (high ROA, low NPF) are considered to be institutions that successfully comply with prudential regulations (OJK). Furthermore, transparent Sharia Compliance MR practices are evidence that these LKS have Sharia integrity (Mas'ut, 2023). The integration of these two aspects creates strong institutional legitimacy, attracting more investors and depositors, thereby strengthening the position of LKS as a major pillar of the national economy, as seen in the rapid growth of assets post-consolidation in Indonesia.

Argumentatively, the most important impact is on Institutional Legitimacy. Compliance with OJK and DSN-MUI regulations, as evidenced by stable financial performance, builds public trust, which is the most important currency for LKS. The stability demonstrated through good MR reassures customers that their funds are managed prudently and in accordance with Sharia law, fundamentally distinguishing LKS from unregulated non-bank financial entities or illegal Fintech.

Therefore, the Results and Discussion conclude that the quality of LKS is a linear function of the integrity of this system: Regulation provides the roadmap and sanctions; MR is the engine that implements it; and Impact is the tangible proof that LKS is capable of achieving its twin goals: profitability and Sharia compliance.

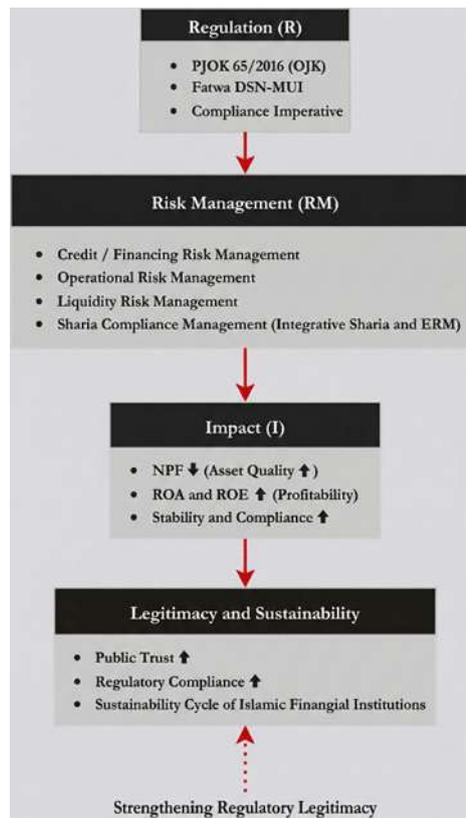


Figure 3. Model Design of the Impact of Regulations on Risk Management Practices in Islamic Financial Institutions

The causal relationship in this model design is formed through three main streams that describe the dynamics between Regulations (R) as an external imperative, Risk Management (RM) as an internal mechanism, and Impact (I) as an institutional output. These three streams form what is known as the Trinity of Islamic Financial Institutions, which emphasizes that the stability and legitimacy of Islamic financial institutions depend on the synergy between regulatory pressure, effective risk management, and measurable performance results.

Stream I: Regulation as a Risk Management Imperative (R→RM)

Regulation is not only regulatory (regulative control), but also forces the establishment of a comprehensive risk management system. OJK Regulation (POJK No. 65/2016) explicitly requires Islamic financial institutions to establish risk management structures and processes for eight main types of risk, thus serving as a formal trigger for the implementation of RM.

Sharia regulations (DSN-MUI) add the dimension of Sharia Compliance Risk, which is unique and not found in conventional systems. This dimension moderates the implementation of RM through the need for alignment between sharia compliance and effective risk management.

These conditions require the adoption of an integrative model such as Integrative Sharia and ERM (Enterprise Risk Management) (Mas'ut, 2023; Fauzi & Maghfiroh, 2025), which integrates the prudential principle and sharia compliance into a single managerial framework.

Flow II: Risk Management as a Determinant of Impact (MR→D)

The effectiveness of MR implementation is a major determinant of the performance and stability of Islamic financial institutions. Credit/Financing Risk Management plays a role in minimizing the ratio of non-performing financing (NPF), which is a direct indicator of asset quality and financial health (Ayu Wandhini, 2024; Sudanto, 2024). Risk Management of Operations and Liquidity supports cost efficiency and smooth cash flow, which ultimately increases profitability (ROA and ROE) (Fauzi & Maghfiroh, 2025; Noory et al., 2021). Thus, RM serves as an institutional adaptation mechanism that transforms potential losses (risk exposure) into financial stability and resilience.

Path III: Impact as a Source of Legitimacy (Feedback)

Positive impacts in the form of low NPF, high ROA/ROE, and consistent sharia compliance become a source of institutional legitimacy. Good performance not only indicates internal effectiveness but also strengthens the trust of regulators, customers, and stakeholders. In the long term, this legitimacy strengthens institutional sustainability, creating positive feedback for regulatory compliance.

6. Conclusion

Regulations serve as the main pillar that encourages and integrates risk management (RM) practices in Sharia Financial Institutions (SFIs). Although this industry is growing rapidly, high growth is risky without a strong managerial framework. Therefore, the Financial Services Authority (OJK) and the National Sharia Council-Indonesian Ulama Council (DSN-MUI) have issued complementary regulations. OJK regulations require the implementation of Enterprise Risk Management (ERM) to manage eight types of financial risks. Meanwhile, DSN-MUI regulations ensure that LKS mitigate sharia compliance risks, which are unique and fundamental risks. Dual compliance with these regulations is not only a legal obligation but also serves as a strategic guide that ensures Islamic Financial Institutions operate prudently and in accordance with sharia principles.

Thus, risk management is not merely an operational process, but a vital mechanism that translates regulatory mandates into tangible performance. Effective MR implementation, such as minimizing the Non-Performing Financing (NPF) ratio and increasing profitability (ROA/ROE), directly reflects the success of LKS in managing risk complexity. This solid performance ultimately builds institutional legitimacy and public trust. Therefore, the relationship between regulation, risk management, and performance is a reinforcing cycle, where good regulation encourages sound risk management practices, which in turn generate positive and sustainable impacts for Islamic Financial Institutions as a whole.

Limitations

This study acknowledges several limitations that should be considered when interpreting the findings. First, employing a Systematic Literature Review (SLR) methodology, this analysis relies exclusively on secondary data from published articles; consequently, it lacks direct empirical verification or field observations to discern the nuances between formal administrative compliance and actual operational practices. Second, the geographical and regulatory scope is specifically confined to the Indonesian context, focusing primarily on regulations from the Financial Services Authority (OJK) and fatwas from the National Sharia Council (DSN-MUI), which may limit the generalizability of the findings to jurisdictions operating under different Sharia governance frameworks. Third, the data selection process was restricted to 34 articles published between 2019 and 2025 using specific keywords, raising the possibility that relevant literature falling outside these inclusion criteria or internal policy documents not published academically may have been excluded.

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