

The future of cryptocurrencies from the perspective of Islamic economics

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Abstract---This presentation addresses the study of the future of cryptocurrencies in the context of Islamic economics, considering the challenges and opportunities arising in this field. Having emerged in the last two decades, cryptocurrencies threaten the traditional financial system. However, there are fundamental questions regarding their compliance with Islamic economic principles, which prohibit usury (riba) and uncertainty (gharar). While cryptocurrencies offer significant opportunities to facilitate access to financing in countries with weak banking systems, the challenge lies in their high volatility and lack of compatibility with traditional banking systems. The presentation also discusses the necessity of creating Sharia-compatible legislation to ensure the safe use of cryptocurrencies. One possible approach would be to regulate cryptocurrencies by linking them to essential commodities such as gold or oil, or by issuing them through central banks. Cryptocurrencies present a dual challenge and opportunity to the Islamic economy. As these currencies evolve and Islamic financial institutions become more interested in financial technology, they are expected to play a more significant role in the Islamic financial system — provided they are adapted according to Sharia principles.

Keywords---Cryptocurrencies, Islamic economics, Bitcoin.

Introduction

Over the past two decades, cryptocurrencies have emerged as one of the most significant financial innovations, transforming the global financial system. Currencies such as Bitcoin, Ethereum and Litecoin represent part of this digital shift, providing an alternative to the traditional financial system which relies on fiat currencies issued by central banks. However, the emergence of cryptocurrencies raises many questions and concerns in both economic and Islamic legal contexts.

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Islamic economics differs from traditional economics in several fundamental ways, such as its prohibition of usury (riba) and financial practices that contradict the principles of social justice and transparency. Thus, dealing with cryptocurrencies in Islamic economics requires an in-depth study, as these currencies are viewed from two main perspectives: the first concerns their permissibility from a Sharia standpoint; the second concerns their applications and potential impact on the future of the Islamic financial system. The issue addressed in this presentation is therefore: to what extent can cryptocurrencies be utilised to develop the future of Islamic economics within its Sharia frameworks and principles?

This scientific presentation studies the future of cryptocurrencies within the framework of Islamic economics, focusing on the challenges, opportunities and expectations these currencies may face in light of Islamic economic principles. It outlines the following sections:

1. Chapter One: Definition of cryptocurrencies and related terms
2. Chapter Two: Islamic economics and cryptocurrencies
3. Chapter Three: Sharia analysis of cryptocurrencies
4. Chapter Four: The Impact of Cryptocurrencies on the Islamic Financial System
5. Chapter Five: The Future of Cryptocurrencies in Islamic Economics

Chapter One: Definition of Cryptocurrencies and Related Terms

Section One: Definition of Cryptocurrencies:

Cryptocurrencies are digital assets that use encryption to ensure the security of financial transactions. They rely on blockchain technology to store and verify data. The most famous and widely used cryptocurrency is “Bitcoin”, but there are many others, such as “Ethereum”, “Ripple” and “Litecoin”. These currencies are traded on specialised platforms and can be used as a medium of exchange or as an investment tool.

Blockchain technology:

Blockchain is the foundational technology used by cryptocurrencies. It is a decentralised digital ledger that stores transactions across a network of interconnected nodes (computers). This technology ensures the security and transparency of transactions, reducing the need for traditional intermediaries such as banks¹.

Blockchain is defined as a distributed database that can manage an ever-growing list of records, known as ‘blocks’, where each block contains a timestamp and a link to the previous block. Blockchains are designed to maintain stored data and prevent it from being altered. The chosen definition is: ‘It is a database that is both size- and time-restricted, consisting of blocks derived from encrypted data that cannot be modified.’²

Section Two: Related Terms

In the course of researching cryptocurrencies, researchers encounter a wealth of closely related or similar terminology. Understanding these terms is essential in order to clarify their meanings and recognise the differences between them. Some economic analysts and financial experts use terms such as ‘digital currencies’, ‘electronic money’ and ‘virtual currencies’ interchangeably.

First: Definition of electronic money:

Electronic money refers to currencies that require electronic devices, such as computers and card readers, for transactions. The European Commission defines it as follows: ‘Monetary value stored electronically on an electronic medium, such as a card or computer memory, which is accepted as a

¹- Abdul Salam Yasser bin Abdul Rahman, 'Virtual Currencies', Research Excellence Centre, Imam Muhammad bin Saud Islamic University, 2018, p. 2.

²- Osama As'ad Abu Hussein, 'The Legal Ruling on Dealing with Virtual Currencies', article from the proceedings of the conference on virtual currencies, 16–17 April 2019, p. 118.

means of payment by entities other than the institution that issued it. It is made available to users as an alternative to fiat currencies for the purpose of making electronic transfers of a specified value.³

Many studies and pieces of research are titled 'electronic money', and this term was first applied to the credit balance on various types of card, which corresponds to a real monetary value. However, with the emergence of virtual and encrypted currencies, some refer to them as 'electronic', necessitating clarification of the overlap between the terms to elucidate the true meaning of each.

In summary, the relationship between electronic money and cryptocurrencies can be described as follows:

Electronic money has real monetary value stored electronically, whereas virtual currencies are encrypted digital currencies that exist on electronic media or personal computer memory and have no physical existence or intrinsic value. They do not include coins or paper money; rather, they are akin to a Word or Excel file⁴.

Electronic currencies allow users to freeze financial transactions at the request of a participant or the authorities, or if fraud or money laundering is suspected. Virtual currencies, on the other hand, conduct financial transactions through a distributed network of computers, known as peers or nodes, within a global network. These transactions cannot be cancelled, halted or investigated⁵.

Electronic money can be utilized for transactions through the internet and other dedicated electronic devices, making it the fastest and best option for settling the prices of goods and services in e-commerce. In contrast, virtual currencies can only be utilized for benefits through the internet, which means it is impossible to exchange this currency if the internet is disrupted⁶.

Electronic money is subject to regulation, which allows users, recipients, transfer mechanisms and amounts sent to be identified. This prevents its use in smuggling and money laundering operations. Conversely, virtual currencies are unregulated and can be used for illicit activities such as financing terrorism and money laundering⁷.

Second: digital currencies

This contemporary term is also referred to as digital money. The European Central Bank defines it as follows: 'A type of unregulated digital money, usually issued and controlled by developers, and used and accepted among members of a specific virtual community.'⁸ In 2013, the U.S. Department of the Treasury defined it as: 'A medium of exchange that acts as a currency in certain contexts, but does not possess all the properties of real currency.'⁹

Section Three: Characteristics of Cryptocurrencies

Decentralisation: There is no central authority controlling cryptocurrencies, which grants them financial independence.

Ease of use: They facilitate the transfer of money from one country to another in a matter of seconds, making transactions instantaneous and time-efficient.

³- Hashem Nasruddin Suwaidan, 'The Legal Regulation of Electronic Money: A Comparative Study', Master's thesis, An-Najah National University, Nablus, Palestine, 2022, p. 13.

⁴- Mohamed Saad Al-Jarf, 'The Impact of Using Electronic Money on Demand for Goods and Services', Proceedings of the Conference on Electronic Banking between Sharia and Law, Vol. 1, 2003, United Arab Emirates University, p. 196.

⁵- See: Shaima Joudat Magdy, 'The Rulings on Dealing with Electronic Money and Its Impact on Contemporary Transactions', Master's thesis, Islamic University of Gaza, 2015, p. 46 onwards.

⁶- Nabil Al-Arabi, 'The Electronic Check and Digital Money', in Proceedings of the Conference on Electronic Banking between Sharia and Law, Vol. 1, United Arab Emirates University, 2003, p. 71.

⁷- Ali Al-Qaradaghi, Digital Electronic Currencies, p. 5.

⁸- Quoted from bit-chain.com, 'Bitcoin: The Currency That Will Change the World', 28/08/2017.

⁹- See eumlat.net.

- Lower costs: service fees are significantly lower than those charged by banks and for real-world transfers.
- Transparency: All transactions are recorded on the blockchain, ensuring transparency and accountability.
- Security: Complex encryption and decentralisation make them more secure than traditional financial systems.
- Volatility: Cryptocurrencies exhibit significant fluctuations in value, which can present challenges for investors and users¹⁰.

Chapter Two: Islamic Economics and Cryptocurrencies

First: Fundamental Principles of Islamic Economics:

- Prohibition of Riba (Usury): Riba is the unjustified increase in the value of loans and is forbidden by Islamic law, as stated in the Quran: ‘Allah has permitted trade and forbidden usury.’
- Prohibition of Gharar (Uncertainty): Transactions involving uncertainty or ambiguity, such as gambling or opaque dealings, are forbidden in Islamic economics.
- Achieving social justice: Islamic economics aims to distribute wealth fairly and encourages investments that benefit society.
- Principle of Economic Freedom:¹¹ This refers to the freedom to own and manage one’s own projects, and to engage in trade and financial activities in accordance with specific Sharia guidelines set out in the Quran and Sunnah.

Second: challenges posed by cryptocurrencies to Islamic economics:

- Riba and financial transactions: cryptocurrencies themselves do not carry usurious interest, but they are primarily used in speculative trading or short-term investments that may indirectly involve riba if financed through usurious instruments.
- Gharar and risks: the sharp fluctuations in the value of cryptocurrencies make it difficult to establish a stable value, which can lead to uncertainty or gharar in transactions and contradicts Sharia principles that emphasise clarity in dealings.
- Uncertainty in Sharia compliance: Although cryptocurrencies may provide an alternative to traditional payment methods, there is divergence of opinion among scholars regarding their permissibility, creating uncertainty for Islamic financial institutions.

Chapter Three: Sharia Analysis of Cryptocurrencies:

Section One: Positions of Scholars Regarding Cryptocurrencies:

Although some scholars believe that cryptocurrencies do not contradict Islamic law, their views on their use differ. Opinions range from:

First: Fatwas declaring prohibition:

Proponents of this view argue that the sharp fluctuations in cryptocurrency values may represent gharar (uncertainty), contradicting the principles of transparency and justice in financial transactions. Among the fatwas that state prohibition are:

1. Fatwa of the International Union of Muslim Scholars:

Decision No. 1 for the year 1444 AH, issued by the Ijtihad and Fatwa Committee of the International Union of Muslim Scholars, states the following regarding dealing with Bitcoin and other digital currencies: ‘It is not permissible to deal in Bitcoin and other “unofficial” digital currencies in their current form, nor to trade or manufacture them.’

The committee presented several reasons for this decision, including the fact that they do not meet the characteristics of currencies or the conditions of money, as defined by scholars, economists and others.

¹⁰. Tawfiq Azraq, ‘The General Characteristics of the Islamic Economy and Its Most Important Governing Principles’, December 2020, <https://www.researchgate.net/publication/361903460>.

¹¹. Website of the International Union of Muslim Scholars, short link: <https://iums.me/26607>.

These reasons include the fact that they should govern and mediate among all other forms of wealth in order to establish value; that they have no intrinsic purpose; and that their relationship to other forms of wealth is identical¹².

2. Fatwa of the Egyptian Fatwa House:

Dr Shawki Allam stated that engaging with Bitcoin, conducting transactions through it (such as buying, selling or leasing) and participating in it is prohibited due to its lack of recognition as an acceptable medium of exchange by competent authorities. This is in addition to the harms arising from gharar (uncertainty and deceit) regarding its usage and value, and the high risks it poses to individuals and nations¹³.

3. Fatwa of the Islamic Fatwa Council in the State of Palestine:

This fatwa is titled “The Islamic Fatwa Council Issues a Fatwa Prohibiting Dealings in Bitcoin and Other Cryptocurrencies,” stating: “Based on the above, since Bitcoin has no physical existence and is not linked to official financial institutions or intermediary financial entities such as banks, and it is not subject to regulatory authority, this currency does not meet the conditions considered for real currencies; it does not achieve value and is not suitable to be used as a measure for the prices at which goods are evaluated. Therefore, it is not permissible to deal with this currency as it is not a currency recognized by Sharia, and due to the gharar and uncertainty it entails that leads to the loss of the rights of many people and unjust consumption of their wealth. Uncertainty surrounds Bitcoin from all sides: it relies on encryption principles in all aspects, and the laws governing it do not include any information about the person or their data; uncertainty accompanies it from the moment of acquisition and usage.

Furthermore, dealing with other cryptocurrencies is also not permissible because they lack a tangible, physical entity or existence. According to a narration in Sahih Muslim from Abu Huraira, the Messenger of Allah (peace be upon him) prohibited the sale of gharar. The Ummah consensus is that only known items can be sold for known items. Even now, the nature of these encrypted currencies remains uncertain: are they a commodity, a service, a financial investment asset, or a digital asset? Are cryptocurrencies considered valuable and tradable under Sharia law?¹⁴

Secondly, fatwas permitting their use:

Some scholars believe that cryptocurrencies are not prohibited because they do not inherently involve riba or prohibited transactions, and they may serve as a means of financial exchange. Among these scholars is Dr Nayef Al-Ajmi from Kuwait¹⁵.

Having presented the fatwas of various scholars on these cryptocurrencies and digital currencies, I am convinced that these currencies are a contemporary issue imposed by the passage of time. This requires Muslim scholars to adapt and utilise them effectively to serve the economy of the Islamic Ummah. It is inevitable that we will have to deal with them in the future, especially given the current circumstances of Muslims, which reflect a state of being overwhelmed. We anticipate leveraging these scholarly platforms to find Sharia-compliant solutions for dealing with these virtual currencies in the future, in accordance with the principles of Islamic economics. Therefore, we propose a set of Sharia standards for cryptocurrencies.

Section Two: Sharia Standards Required for Cryptocurrencies

First: Non-contradiction with Quranic texts and the Sunnah:

Cryptocurrencies must adhere to the principles of Islamic economics, including avoiding riba (usury), gharar (uncertainty) and prohibited activities.

Secondly, safe and transparent trading is required.

Guarantees are essential to protect transactions and avoid fraud or money laundering.

Thirdly, compliance with social objectives is required.

¹². Official website of the Egyptian Fatwa House: <https://www.dar-alifta.org/ar>, published 2 January 2018.

¹³. <https://www.fatawah.net/Fatawah/1236.aspx>

¹⁴. <https://www.fatawah.net/Fatawah/1236.aspx>

¹⁵. The Juridical Adaptation and Legal Ruling on Cryptocurrencies', Dr Naif Al-Ajmi, <https://www.youtube.com/watch?v=UiZx0R-K7fE>.

Cryptocurrencies should contribute to achieving economic justice, enhancing community welfare and preventing the exploitation of the poor and needy.

Chapter Four: The impact of cryptocurrencies on the Islamic financial system

Section One: Opportunities offered by cryptocurrencies for Islamic financing.

First: Expanding access to financing:

Cryptocurrencies can provide individuals and businesses in countries with weak banking systems with access to financing.

Secondly, cryptocurrencies can help to achieve transparency.

Through blockchain technology, cryptocurrencies can ensure greater transparency in financial transactions, helping to avoid corruption and fraud.

Thirdly, the possibility of implementing smart contracts:

Smart contracts on the blockchain can be used to finance projects that comply with Islamic law, such as profit-sharing and partnerships. This makes the execution of these contracts more precise and secure.

Section Two: Economic Challenges of Cryptocurrencies:

First: Price volatility:

Although cryptocurrencies offer new possibilities, their significant value fluctuations make them unsuitable for daily transactions.

Secondly, cryptocurrencies are incompatible with traditional banking systems.

Cryptocurrencies do not always align with the traditional financial system based on banks, which may lead to limited acceptance in some markets.

Chapter Five: The Future of Cryptocurrencies in Islamic Economics

Section One: Future Developments

First: Growth of Islamic Cryptocurrencies:

A new type of cryptocurrency that fully complies with Sharia law principles may emerge in the future, such as digital currencies developed by Islamic financial institutions.

Secondly, cooperation between Islamic banks and crypto platforms may increase.

In the coming years, we may see Islamic banks cooperate with digital platforms that manage cryptocurrencies to create Sharia-compliant solutions.

Section Two: Regulation and Legislation

To ensure the safe and legitimate use of cryptocurrencies, it is important to develop regulations and legislation that comply with Sharia. Islamic financial institutions will need to update their legal frameworks to include cryptocurrencies, specifying the circumstances in which they can be used and defining their limits. Some contemporary scholars have proposed various alternatives to correct the trajectory of virtual currencies and transition them from prohibition to permitted use. These alternatives include:

First, linking them to more stable and secure assets, such as tying them to oil, gas or other gold-backed commodities, to achieve relative stability.

Second, having them issued by an international or global central bank. When the price of the digital currency starts to rise, the production rate increases, flooding the market and bringing prices down. Conversely, when prices start to fall, the bank begins to buy back the issued currencies, reducing their market supply and increasing their price.

Thirdly, a country could adopt them as a secondary currency. This would give the currency official and central status, applying the same Sharia rulings as those applied to other currencies linked to gold, silver and other commodities.

Fourth: Issuing credit cards with advanced technology linked to central banks or establishing a joint-stock company whose assets could include commodities, gold, etc., organised in a specific manner with

technical efforts directed towards digital shares or the issuance of electronic sukuk based on these currencies for current or future projects.

Fifthly, the union of three virtual currencies operating as one currency. James Zderalick suggested this solution, envisaging these three symbolic currencies as being based on traditional digital currencies, which in turn are based on the productivity or outputs of countries. The first of these symbolic currencies would be tied to shares representing ownership rights in a factory. The second would be based on a company's inventory, granting its owners rights to that inventory. The third symbolic currency would be the sum of the first two¹⁶.

Section Three: Central Bank Digital Currencies (CBDC)

Although decentralised cryptocurrencies present several challenges, central banks in many countries are suggesting Central Bank Digital Currencies (CBDCs) as an alternative. These currencies are expected to be more compatible with traditional financial systems and could solve several issues associated with cryptocurrencies, particularly with regard to oversight and compliance with legal frameworks.

CBDCs are digital currencies issued and managed by the central banks of specific countries. Unlike other digital currencies, they are not subject to the decentralisation process that characterises the ecosystem of other digital currencies.

In a report published in 2022, the Bank for International Settlements defined central bank digital currencies as follows: 'A digital payment instrument denominated in the national unit of account that is a direct liability of the central bank and legally tendered as a medium of exchange and a store of value, with a unit of account equivalent to that of the fiat currency.'¹⁷

Conclusion:

Cryptocurrencies present a dual challenge and opportunity for Islamic economics. While they offer significant potential to enhance transparency and financial justice, they face many challenges in terms of compliance with Sharia principles, particularly with regard to *riba* (usury) and *gharar* (uncertainty). As interest in fintech grows within the Islamic world, it is expected that cryptocurrencies will evolve to become part of the Islamic financial system, provided they are adapted to align with Islamic law and meet the needs of the Muslim community.

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¹⁶ See: Ali Mohiuddin Al-Qaradaghi, Digital Electronic Currencies, p. 30 and beyond. Abu Ghuda, Digital Money, p. 24 and beyond. Ismail Al-Jamili, Virtual Currencies, p. 92.

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