At-Tahdzib: Jurnal Studi Islam dan Mu'amalah
Volume 14 Nomor 1, Maret 2026
DOI: https://doi.org/10.61181/g0cemc13

ISSN (Cetak) : 2089-7723
ISSN (Online) : 2503-1929

Dynamic Capability-Based Mitigation of Displaced Commercial Risk in the Management of Temporary Syirkah Funds in Islamic Banks

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Abstract

Background. *This study presents an in-depth conceptual analysis of strategies for mitigating Displaced Commercial Risk (DCR), one of the most fundamental and distinctive risks faced by Islamic banks operating within a dual banking system. DCR refers to the situation in which Islamic banks are compelled to provide investment returns to depositors that do not accurately reflect the actual performance of the underlying assets in order to maintain market competitiveness.*
Aim. *Consequently, this practice inherently undermines the fundamental principle of Profit and Loss Sharing (PLS) that distinguishes Islamic banking from conventional banking.*
Methods. *Employing a qualitative conceptual approach through critical analysis and literature synthesis, this study deconstructs the limitations of the prevailing mitigation paradigm, which relies heavily on reactive instruments such as the Profit Equalization Reserve (PER).*
Results. *As its primary contribution, this study proposes a Dynamic Capability Framework for DCR Mitigation. Rather than viewing DCR mitigation as a purely technical risk management function, the proposed framework conceptualizes it as a core organizational capability that Islamic banks must continuously develop and strengthen. The framework comprises three interrelated capability pillars: Sensing Capability, which identifies market volatility and asset-related risks; Seizing Capability, which responds proactively through effective Asset–Liability Management (ALM) and adaptive reserve management; and Transforming Capability, which enhances long-term organizational resilience through product innovation and stakeholder expectation management.*

Keywords: *Displaced Commercial Risk; Temporary Syirkah Funds; Profit Equalization Reserve; Dynamic Capabilities; Risk Management; Islamic Banking*

INTRODUCTION

The existence and continuous growth of the global Islamic banking industry are founded upon a distinctive and fundamental value proposition: conducting financial intermediation based on the principles of justice, transparency, and PLS. Theoretically, these principles distinguish Islamic banking fundamentally from the conventional interest-based banking system. In practice, however, Islamic banks do not operate in isolation. They function within a dual banking system, where market expectations, performance benchmarks, and competitive dynamics continue to be largely shaped by conventional banking practices.[1]

This environment creates a persistent strategic dilemma for Islamic banks. They are required to simultaneously maintain Shariah compliance, market competitiveness, and financial stability—three objectives that frequently conflict with one another. The tension becomes particularly evident in the management of investment accounts, commonly referred to as Temporary Syirkah Funds, such as Mudarabah investment deposits. According to Shariah principles, the returns distributed to investment

[1] Habibi et al., "Challenges and Adaptation Strategies of Mosque Takmirs in the Transition from Conventional Reporting to Accounting Strandards Based on PSAK 45 and PSAK 101."

ISSN (Cetak) : 2089-7723
ISSN (Online) : 2503-1929

account holders should directly reflect the actual performance of the underlying investment assets. In reality, however, customers often compare these returns with the relatively stable and predictable interest rates offered by conventional banks.[2]

This tension gives rise to a unique and inherent risk within Islamic banking known as DCR. DCR refers to the commercial risk transferred from investment account holders (IAHs) to the Islamic bank when the bank sacrifices part of its own profit – or even shareholders' returns – to provide investment returns that remain competitive with those of conventional banks.[3] Although this practice is often considered necessary to retain depositors in a highly competitive market, it constitutes a significant deviation from the fundamental philosophy of PLS. Consequently, DCR threatens not only the financial stability of Islamic banks through potential capital erosion but also gradually weakens the philosophical foundation of Islamic banking, making it appear merely as conventional banking operating under a Shariah label.[4]

Despite being widely recognized as an inherent risk in Islamic banking – as reflected in standards issued by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) – academic and practical discussions have largely concentrated on a single mitigation instrument, namely the PER. Existing studies predominantly focus on the accounting treatment and Shariah legitimacy of PER, while relatively few critically evaluate its effectiveness and limitations as a long-term strategic solution. Consequently, there remains a significant gap in the literature concerning DCR from the perspective of strategic management, where it should be understood as a complex organizational challenge requiring solutions beyond technical accounting mechanisms.[5] This study aims to address the aforementioned gap by providing a comprehensive and multidisciplinary analysis of DCR mitigation. The novelty of this research lies in three principal contributions.[6]

First, from an analytical perspective, this study critically deconstructs the prevailing PER-centered mitigation paradigm by identifying its inherent limitations and the secondary risks it may generate, particularly moral hazard.

Second, from a theoretical perspective, this study introduces and adapts the Dynamic Capabilities View (DCV) proposed by Teece, Pisano, and Shuen as a new conceptual lens for understanding and formulating DCR mitigation strategies.[7] This represents a significant conceptual advancement, shifting the perspective from viewing DCR mitigation as a static technical function toward recognizing it as a dynamic organizational capability.[8]

Finally, as its primary contribution, this research develops an Integrated Dynamic Capability Framework for DCR Mitigation. Unlike existing reactive and symptom-oriented approaches, the proposed framework offers a holistic, proactive, and strategically integrated model for managing DCR while simultaneously preserving competitiveness, financial resilience, and Shariah compliance within Islamic banking institutions.[9]

REVIEW LITERATUR

The Nature of Temporary Syirkah Funds and the Issue of Rate of Return Smoothing

Temporary Syirkah Funds mobilized through Mudarabah and Musyarakah contracts represent investment-based funding sources that differ fundamentally from conventional deposit accounts. Rather than establishing a debtor–creditor relationship, these contracts create a partnership between the

[2] Al-Azhar et al., "The Impact of the Financial Sector Development and Strengthening Law (UUP2SK) on the Supervision of Islamic Microfinance Institutions."

[3] Archer, S., & Karim, R. A. A. (2007). *Islamic finance: The regulatory challenge*. John Wiley & Sons.

[4] Nasirin et al., "Peran Informasi Harga Dalam Mempengaruhi Keputusan Konsumen Di Pasar Mikro."

[5] Habibi et al., "Challenges and Adaptation Strategies. *Ibid*.

[6] Hidayati et al., "Optimalisasi Insentif Pajak Terhadap Instrumen Sukuk Ijarah Dalam Pengembangan Pasar Modal Syariah Indonesia."

[7] Teece, D. J., Pisano, G., & Shuen, A. (1997). Dynamic capabilities and strategic management. *Strategic Management Journal,* 18(7), 509–533.

[8] *Ibid*.

[9] Ahmad et al., "Corporate Disclosure : Upaya Mengatasi Asimetri Informasi Pedagangan Online."

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investment account holder (*shahibul mal*) and the Islamic bank (*mudharib*), whereby profits are distributed according to a pre-agreed profit-sharing ratio, while losses are allocated in proportion to capital contributions, subject to the respective managerial responsibilities of each party.[10] Consequently, variability in investment returns is an inherent feature of this contractual arrangement, implying that the returns received by investment account holders should reflect the actual performance of the bank's financing portfolio.[11]

Despite this theoretical framework, return volatility poses a significant competitive challenge for Islamic banks because investment account holders often benchmark their returns against the relatively stable interest rates offered by conventional banks. To address this challenge and reduce the risk of fund withdrawals, many Islamic banks engage in rate of return smoothing through mechanisms such as the PER. Under this approach, a portion of profits generated during periods of strong financial performance is retained and subsequently used to stabilize returns during less profitable periods, thereby reducing fluctuations in payouts to investment account holders.[12]

The practice of return smoothing has attracted considerable attention in the Islamic finance literature. Proponents argue that it protects investment account holders from excessive return volatility, enhances depositor confidence, and contributes to both institutional resilience and financial system stability.[13] In contrast, critics maintain that excessive smoothing undermines transparency, weakens market discipline, and dilutes the genuine risk-sharing nature of Islamic finance by making PLS investment accounts increasingly resemble conventional interest-bearing deposits. Such practices are therefore viewed as inconsistent with the fundamental principles of Shariah, which prohibit the guarantee of investment returns and require returns to be linked to the actual performance of underlying economic activities.[14]

DCR: Anatomy and Systemic Implications

DCR represents the most visible manifestation of the challenges associated with rate of return smoothing in Islamic banking. It emerges when Islamic banks voluntarily absorb part of the investment risk that should legitimately be borne by investment account holders in order to maintain competitive investment returns.[15]

The mechanism underlying DCR can be understood through the following causal sequence. First, the performance of assets financed by Temporary Syirkah Funds deteriorates, resulting in lower investment returns.[16] Second, conventional deposit interest rates remain stable or increase, creating market expectations regarding a minimum acceptable level of returns. Third, fearing substantial withdrawals of investment funds and the potential loss of market share, the management of the Islamic bank decides not to reduce the profit-sharing distribution proportionately to the decline in asset performance.[17] Fourth, the difference between the return that should have been distributed according to the actual investment performance and the return ultimately paid to customers is absorbed by the bank itself, typically at the expense of shareholders' profits. Finally, if this practice continues over an extended

[10] Archer, S., & Karim, R. A. A. *Ibid*.

[11] Ahmad et al. *Ibid*.

[12] Abidin et al., "Pengukuran Kinerja Keuangan Organisasi Islami Non Profit : (Studi Kasus Di BAZNAS Kabupaten Jombang)."

[13] Zarqa, M. A. (1983). Stability in an interest-free Islamic economy: A note. *Pakistan Journal of Applied Economics*, 2(2), 181–188.

[14] Chapra, M. U. (2008). The global financial crisis: Can Islamic finance help? In H. Visser (Ed.), *Islamic economics and finance: A European perspective* (pp. 41–54). Edward Elgar.

[15] Hidayati et al., "Optimalisasi Insentif Pajak Terhadap Instrumen Sukuk Ijarah Dalam Pengembangan Pasar Modal Syariah Indonesia."

[16] Husen et al., "Empowerment of UP2K Cadres through the Sharia Financial Literacy Program as an Effort to Strengthen MSMEs in Sajen Village, Pacet District, Mojokerto Regency."

[17] Ahmad, "Analisis Kaidah Ushul Fiqh Dalam Menyikapi Inovasi Produk Ekonomi Digital Syariah."

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period or occurs during severe economic downturns, it may significantly erode the bank's profitability and capital base.[18]

The consequences of DCR extend beyond individual institutions and possess systemic implications. At the institutional level, DCR increases both profitability and solvency risks because shareholders bear losses that should ordinarily be shared with investment account holders. At the industry level, persistent reliance on DCR undermines the credibility of the PLS model, which constitutes the defining feature of Islamic banking. This phenomenon creates a self-reinforcing cycle. In order to remain competitive, Islamic banks increasingly imitate conventional banking practices. As this imitation becomes more widespread, the distinctive characteristics of Islamic banking gradually diminish, thereby weakening its competitive differentiation and long-term value proposition.[19]

A Critical Assessment of the PER: Solution or Illusion?

PER is the most widely adopted mechanism for mitigating DCR. It is established by allocating a portion of gross income during periods of strong financial performance, which can subsequently be utilized to stabilize investment returns during periods of weaker performance.

Although PER is recognized within the AAOIFI standards as a permissible risk management instrument, excessive dependence on this mechanism raises several fundamental concerns. First, PER essentially functions as a symptomatic treatment rather than a genuine solution.[20] It addresses the immediate symptom – namely, uncompetitive investment returns – without resolving the underlying causes, such as poor asset quality, inadequate portfolio diversification, or ineffective financing strategies.[21] Consequently, it may conceal structural weaknesses within the bank's asset portfolio rather than encourage meaningful improvements. Second, excessive reliance on PER may create dual moral hazard.[22] From the management perspective, the existence of substantial reserves may reduce incentives to strengthen asset quality, improve financing selection, and enhance portfolio monitoring.[23] The availability of financial buffers can unintentionally encourage complacency in risk management practices. From the customers' perspective, consistently stable investment returns may foster the misconception that Temporary Syirkah Funds are essentially risk-free investment products. This perception fundamentally contradicts the essence of the PLS principle and diminishes customers' understanding of investment risk in Islamic finance. Third, PER is inherently a finite resource. Reserve accumulation depends upon favorable financial performance and cannot expand indefinitely. During prolonged economic downturns or financial crises, accumulated reserves may become exhausted. Institutions that rely excessively on PER may therefore find themselves without adequate defensive mechanisms when reserves are depleted. Accordingly, although PER remains a useful tactical instrument for mitigating short-term return volatility, it should not be regarded as a comprehensive long-term strategy for managing DCR.[24]

Theoretical Foundation: Toward a Dynamic Capabilities Perspective

To overcome the limitations of the prevailing mitigation paradigm, a broader theoretical perspective is required. The DCV, provides a robust conceptual foundation for understanding how organizations sustain competitive advantage in rapidly changing environments. According to the Dynamic Capabilities framework, sustainable competitive advantage does not primarily arise from

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[18] Habibi, Shiddiq, and Ahmad, "Kontribusi Perbankan Syariah Dalam Mendukung Ekonomi Halal Nasional."

[19] Al-Azhar et al., "The Impact of the Financial Sector Development and Strengthening Law (UUP2SK) on the Supervision of Islamic Microfinance Institutions."

[20] Ahmad et al., *Ibid.*

[21] Ilma, Husen, and Abidin, "Arah Kebijakan Hukum Syariah Dalam Menghadapi Tatangan Modernitas Transaksi Non Tunai."

[22] Abidin et al., "Pengukuran Kinerja Keuangan Organisasi Islami Non Profit : (Studi Kasus di BAZNAS Kabupaten Jombang)."

[23] Ahmad et al., *Ibid.*

[24] Habibi et al., "Dekontruksi Perlakuan Akuntansi Dana Syirkan Temporer: Jebakan Hibriditas Dan Hegemoni Paradigma Utang-Ekuitas Konvension."

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possessing valuable resources alone. Rather, it depends on an organization's ability to intentionally build, integrate, and reconfigure internal and external competencies in response to environmental change.[25]

Dynamic capabilities consist of three interrelated organizational capacities. The first is Sensing Capability, which refers to an organization's ability to identify emerging opportunities, anticipate environmental changes, and recognize potential threats before they materialize. The second is Seizing Capability, which concerns the organization's capacity to mobilize resources and implement effective strategic responses that capitalize on identified opportunities while mitigating emerging risks. The third is Transforming Capability, which reflects the organization's ability to continuously renew and reconfigure its asset base, organizational processes, and business models to maintain long-term competitiveness.[26]

Applying this theoretical perspective to Islamic banking suggests that DCR mitigation should no longer be viewed merely as an accounting or treasury function focused on managing instruments such as the PER.[27] Instead, it should be conceptualized as a core dynamic organizational capability that enables Islamic banks to balance Shariah compliance, market competitiveness, and financial resilience in an increasingly complex and competitive banking environment.[28] This perspective shifts the focus from reactive risk management toward proactive organizational adaptation, thereby providing a more comprehensive foundation for achieving sustainable competitiveness while preserving the fundamental principles of Islamic finance.[29]

METHOD

This study adopts a qualitative-conceptual methodology using a critical analysis and theory-building approach. This approach was selected because the objective of the study is not to test hypotheses statistically, but rather to critically deconstruct the existing paradigm and develop a more robust conceptual framework. The research was conducted through three stages: Critical Literature Review and Synthesis, which involved an in-depth examination of the existing literature on DCR, the PER, and Islamic risk management, with particular emphasis on identifying the underlying assumptions, scholarly debates, and existing limitations; Cross-Disciplinary Theoretical Integration, which intentionally adopts and adapts the DCV from the strategic management literature to provide a new analytical perspective, and: Conceptual Deduction and Framework Development, through which a new conceptual model (the principal finding of this study) was logically derived from the results of the critical literature synthesis and theoretical analysis.

RESULT

This section presents a comprehensive discussion of the conceptual arguments developed in this study. It begins with a critical evaluation of the conventional paradigm for mitigating DCR before introducing the proposed Dynamic Capability Framework for DCR Mitigation. The discussion subsequently elaborates on each capability dimension and explains its strategic significance for Islamic banking institutions.[30]

Limitations of the Conventional DCR Mitigation Paradigm: A Critical Evaluation of the Overreliance on PER

[25] Teece, D. J., Pisano, G., & Shuen, A. *Ibid*.

[26] Nasirin et al., "Peran Informasi Harga Dalam Mempengaruhi Keputusan Konsumen Di Pasar Mikro."

[27] Husen et al., "Empowerment of UP2K Cadres through the Sharia Financial Literacy Program as an Effort to Strengthen MSMEs in Sajen Village, Pacet District, Mojokerto Regency."

[28] Zakiyyah Ilma Ahmad, Nur Laily Hidayati, "Analisis Efektivitas Dana Desa dalam Mendukung UMKM Syariah di Daerah Pedesaan."

[29] Abidin et al., "Pengukuran Kinerja Keuangan Organisasi Islami Non Profit: (Studi Kasus di BAZNAS Kabupaten Jombang)."

[30] Kasus et al., "Journal of Economic and Islamic Research Vol. 4 No. 01 November (2025)."

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The prevailing approach to mitigating DCR can be likened to a shock-absorber mechanism. Within this paradigm, the PER functions as a financial cushion that dampens fluctuations in investment returns caused by deteriorating asset performance. While such an approach may temporarily preserve depositor confidence, it fails to address the underlying structural factors responsible for the emergence of DCR. In essence, the conventional approach treats the symptoms rather than the disease itself.[31]

The first major limitation is that excessive reliance on PER creates an illusion of financial stability. By artificially smoothing investment returns, PER conceals valuable market signals that should otherwise prompt corrective managerial actions.[32] Poor financing decisions, deteriorating asset quality, or ineffective portfolio allocation may remain unnoticed because their immediate effects on investment returns are masked by reserve utilization. Consequently, management may delay implementing necessary improvements in financing policies and asset portfolio management. Similar to the use of painkillers for a serious infection, PER alleviates visible symptoms while allowing the underlying problems to persist and potentially worsen.[33]

The second limitation concerns the emergence of dual moral hazard. From a managerial perspective, the availability of substantial reserves may unintentionally weaken incentives to improve asset quality and strengthen financing discipline. Managers may become increasingly reliant on reserve mechanisms rather than pursuing sustainable improvements in financing performance, portfolio diversification, and risk assessment. From the perspective of investment account holders, consistently stable returns may foster unrealistic expectations that Temporary Syirkah Funds are virtually risk-free investment products. Such expectations fundamentally contradict the PLS philosophy, under which both profits and investment risks should be shared fairly between capital providers and entrepreneurs. As a consequence, customers may gradually perceive Islamic investment accounts as conventional deposits with different contractual terminology, thereby eroding the distinctiveness of Islamic banking.[34]

The third limitation arises from the inherently finite nature of PER. Reserve accumulation depends on favorable financial performance and cannot continue indefinitely. During prolonged economic downturns, declining profitability restricts the bank's ability to replenish reserves while simultaneously increasing the need to utilize them. Once reserves are depleted, institutions that depend primarily on PER become considerably more vulnerable because no alternative organizational capabilities have been developed to manage DCR effectively. Taken together, these limitations suggest that PER should be regarded as a supporting tactical instrument rather than the central pillar of DCR mitigation. Sustainable mitigation requires a broader organizational perspective that emphasizes strategic adaptability instead of merely financial buffering.[35]

DISCUSSION

Novel Findings: Developing Dynamic Capabilities for Managing DCR

Recognizing the limitations of the conventional paradigm necessitates a fundamental shift in perspective. Rather than treating DCR mitigation as a reactive technical function performed by treasury or accounting departments, Islamic banks should regard it as a core organizational capability embedded throughout the institution.

Based on the DCV, this study proposes a Dynamic Capability Framework for DCR Mitigation, comprising three mutually reinforcing capabilities: Sensing, Seizing, and Transforming. These capabilities operate sequentially while continuously interacting to enable Islamic banks to anticipate risks, respond strategically to changing market conditions, and strengthen long-term organizational resilience. The proposed framework is illustrated conceptually as follows.[36]

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[31] Husen et al., "Empowerment of UP2K Cadres through the Sharia Financial Literacy Program as an Effort to Strengthen MSMEs in Sajen Village, Pacet District, Mojokerto Regency."

[32] Arifin and Nasirin, "Potensi Ekonomi Syariah Dalam Mendorong Pembangunan Ekonomi Global."

[33] *Ibid.*

[34] Kasus et al., "Journal of Economic and Islamic Research Vol. 4 No. 01 November (2025)."

[35] Maulana et al., "Studi Analisis Peran Perbankan Syari'ah dalam Pengembangan Perekonomian di Pondok Pesantren."

[36] Wahid et al., "Ijtihad Ekonomi Syariah: Telaah Ushul Fiqh terhadap Dinamika Pasar Global."

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Dynamic Capability	Primary Objective	Key Organizational Activities
Sensing Capability	Anticipating and identifying potential DCR	Portfolio risk modeling, market intelligence, depositor behavior analysis
Seizing Capability	Responding strategically to identified risks	Proactive ALM, adaptive reserve management, dynamic profit-sharing policies
Transforming Capability	Building sustainable organizational resilience	Product innovation, stakeholder education, integration of DCR management into organizational culture

Unlike existing approaches that rely heavily on financial reserves, this framework emphasizes organizational learning, strategic flexibility, and continuous adaptation as the principal mechanisms for managing DCR.[37]

Sensing Capability: Anticipating Risks Before They Materialize

Sensing Capability represents an Islamic bank's ability to recognize emerging risks before they develop into significant financial problems. Institutions possessing strong sensing capabilities do not merely react to declining investment returns; instead, they continuously monitor both internal and external environments to identify early warning signals. This capability extends beyond traditional financial analysis by incorporating comprehensive market intelligence and predictive risk assessment.

At the portfolio level, Islamic banks should implement sophisticated stress testing and scenario analysis to evaluate how macroeconomic shocks—including inflation, economic recession, rising financing defaults, or declining sectoral performance—may influence financing portfolios and future investment returns. Simultaneously, competitive market intelligence should encompass not only monitoring competitors' deposit rates but also understanding their strategic behavior, pricing policies, and market positioning. Such information enables Islamic banks to anticipate competitive pressures before they significantly affect depositor decisions.[38]

An equally important component involves analyzing the behavioral sensitivity of investment account holders. Banks should seek to quantify the elasticity of depositor behavior by addressing questions such as: "At what level of return differential are customers likely to transfer their funds to competing institutions?" The answers to these questions provide valuable strategic inputs for subsequent managerial decision-making.[39]

Seizing Capability: Transforming Information into Strategic Action

Once relevant risks have been identified, Islamic banks must possess the organizational capacity to respond effectively. This capability represents the operational core of the proposed framework.

The first strategic response involves proactive ALM. Rather than merely balancing assets and liabilities, ALM should strategically optimize financing portfolios to achieve sustainable risk-adjusted returns while maintaining competitive profit distributions. Portfolio optimization may include increasing financing exposure to sectors demonstrating stable returns with relatively low volatility, improving financing diversification, and actively managing duration mismatches between assets and liabilities.[40]

The second strategic response concerns adaptive reserve and profit distribution management. Within this framework, instruments such as the PER and the Investment Risk Reserve (IRR) remain

[37] Abidin, "Potensi Pemanfaatan Wakaf Tunai Untuk Pembiayaan Startup Bisnis Syariah."

[38] Abidin et al., "Pengukuran Kinerja Keuangan Organisasi Islami Non Profit: (Studi Kasus di BAZNAS Kabupaten Jombang)."

[39] Alazhar, Wahid, and Abidin, "Analisis Faktor Pengambilan Keputusan Strategi Pemasaran BMT Syari'ah di Kabupaten Jombang."

[40] Ahmad, Husen, and Abidin, "Arah Kebijakan Hukum Syariah Dalam Menghadapi Tantangan Modernitas Transaksi Non-Tunai."

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relevant. However, they should operate according to transparent, rule-based governance rather than discretionary managerial decisions. For example, Islamic banks may implement a "traffic-light" policy framework that clearly specifies when reserves may be accumulated, partially utilized, or preserved based on predefined financial indicators. Such governance mechanisms improve transparency, strengthen accountability, and reduce managerial discretion that may otherwise contribute to moral hazard.

Transforming Capability: Building Long-Term Organizational Resilience

Transforming Capability constitutes the highest level of dynamic capability because it enables organizations to continuously reinvent themselves in response to evolving market conditions. Instead of merely adapting existing practices, Islamic banks should redesign their business models to reduce structural dependence on conventional banking benchmarks.

One important strategy involves product innovation. Rather than offering standardized Mudarabah investment accounts, banks could introduce differentiated investment products with varying risk-return profiles.[41] For example, customers may choose between conservative investment accounts emphasizing capital preservation and moderate returns, or growth-oriented investment accounts offering higher return potential accompanied by greater investment risk. Such differentiation allows investment account holders to select products that better align with their individual risk preferences, thereby reinforcing the authentic implementation of PLS principles.[42]

Another equally important strategy involves stakeholder expectation management. Customer education should evolve beyond promotional materials toward integrated communication programs that transparently explain financing performance, investment risks, and the rationale underlying fluctuations in investment returns. Ultimately, the objective is to cultivate a customer base that values Islamic banking because of its distinctive principles rather than because its returns merely resemble those offered by conventional banks. Over the long term, this transformation strengthens customer trust, enhances institutional legitimacy, and reinforces the authenticity of Islamic banking as a genuinely alternative financial system.[43]

CONCLUSION

This study concludes that DCR represents a strategic challenge that extends far beyond a purely technical or accounting issue. Instead, DCR should be understood as a multidimensional organizational phenomenon arising from the inherent tension between maintaining Shariah compliance, preserving market competitiveness, and ensuring financial stability within a dual banking system.

The analysis demonstrates that the prevailing DCR mitigation paradigm, which relies predominantly on reactive financial instruments such as the PER, is insufficient to ensure the long-term sustainability of Islamic banking institutions. Although PER may temporarily stabilize investment returns and reduce competitive pressure, excessive dependence on this mechanism risks concealing structural weaknesses in asset management, creating moral hazard, and gradually undermining the philosophical foundation of the PLS system.

The principal contribution of this study is the development of the Dynamic Capability Framework for DCR Mitigation. Unlike conventional approaches that focus primarily on financial reserve management, the proposed framework conceptualizes DCR mitigation as a core organizational capability requiring continuous development and adaptation.

The framework comprises three mutually reinforcing organizational capabilities: Sensing Capability, which enables Islamic banks to anticipate market changes, identify emerging risks, and monitor depositor behavior proactively; Seizing Capability, which allows banks to respond effectively

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[41] Sunan et al., "Kebijakan Tabungan Perumahan Rakyat Ditinjau Dari Kemaslahatan Umat Menurut Hukum Ekonomi Syariah."

[42] Azhar et al., "Analisis Faktor Pengambilan Keputusan Strategi Pemasaran BMT Syari'ah di Kabupaten Jombang."

[43] Ahmad, Abidin, and Syahni, "Systematic Literature Review: Variable-Variable yang Mempengaruhi Ketaatan Pembayaran Zakat terhadap Keberkahan Zakat Muzakki."

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through proactive ALM, adaptive reserve policies, and dynamic profit-sharing strategies, and; Transforming Capability, which strengthens long-term institutional resilience through continuous product innovation, stakeholder education, and the integration of DCR management into the organization's strategic culture.

Collectively, these capabilities provide Islamic banks with a more sustainable and strategically integrated approach to managing DCR while preserving both competitiveness and Shariah integrity. Accordingly, this study advocates a fundamental paradigm shift—from perceiving DCR mitigation as an isolated technical function toward recognizing it as a dynamic organizational capability that supports sustainable competitive advantage in an increasingly complex financial environment

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