

Comparison of Islamic Unit Trust performance with Conventional

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Abstract. Performance of Islamic Unit trust is a very important issue to Muslims as their concern is not just benefits of this life but also for hereafter. This study investigates whether Islamic unit trust able to outperform conventional. There are 46 Islamic and 53 conventional unit trusts products covering five-year performance has been selected in the study. For comparison purposes, there are five performance measurements has been selected, namely; percentage growth, risk/reward, Sharpe, Treynor and Tracking error. Two Independent samples t test has been employed to assess whether there are differences of mean between Islamic with conventional based on performance measurement respectively. This study found that except for Tracking error, all the performance measurements indicate that conventional unit trusts has outperform Islamic unit trusts significantly.

Introduction

Unit trust investment is one of the mechanism which popular among investors with lots of advantages of investment via unit trust such as the selection of funds are done professionally has encourage investors to put their money in the hand of professional. There are many types of unit trusts products offer in the market which tailor to the return and risk appetite of the investors.

However for Muslimss investors, return and risk is not their only concern as their source of income need to be tally with Allah pleasure. Hereafter life is more important than this worldly life. Islam does not prohibit enjoying worldly life, but it must suit with the teachings of Islam. Therefore, it is very vital for Muslims to invest in Shariah compliance instruments. In Malaysia, Islamic capital markets are under the purview and jurisdiction of Securities Commission (SC) and at the operational level, it is under Bursa Malaysia and Bank Negara Malaysia. SC have established Shariah Advisory Council (SAC) to provide guidelines and as authority body in recognising whether companies' stocks could be classified as shariah compliance or not. SAC has set two main criteria whether a company is consider as shariah compliance, namely, qualitative and financial criteria. Qualitative criteria is concern more on image of the companies, whether it suitable with Islamic image to avoid any Islamic image being tarnish. For an example, a condom company will not get a shariah compliance status even though the products itself is Shariah permissible. Whereas for financial criteria, the SAC looking at two angles; the percentage contribution of non-permissible activities to the group and the contribution of non-permissible funding to the company's source of funds. The table 1 details up criteria under financial criteria evaluation.

Table 1: Financial Screening Criteria

Business Activity Benchmark

Five percent benchmark: -

The five-per cent benchmark is applicable to the following businesses/activities:

- conventional banking, conventional insurance, gambling, liquor and liquor-related activities, pork and pork-related activities, non-halal food and beverages, Shariah non-compliant entertainment, interest and dividend income from conventional accounts and instruments, tobacco and tobacco-related activities; and
- other activities deemed non-compliant according to Shariah.

For the above-mentioned businesses/activities, the contribution of Shariah non-compliant businesses/activities to the overall revenue or profit before taxation of the company must be less than five per cent.

Twenty per cent benchmark

The 20-per cent benchmark is applicable to the following businesses/activities:

- hotel and resort operations, share trading, stockbroking business, rental received from Shariah non-compliant activities; and
- other activities deemed non-compliant according to Shariah.

For the above-mentioned businesses/activities, the contribution of Shariah non-compliant businesses/activities to the overall revenue or profit before taxation of the company must be less than 20 per cent.

Financial Benchmark: -

Cash over total assets

Cash only includes cash placed in conventional accounts and instruments, whereas cash placed in Islamic accounts and instruments is excluded from the calculation.

Debt over total assets

Debt only includes interest-bearing debt whereas Islamic financing or sukuk is excluded from the calculation.

Each ratio, which is intended to measure *riba* and *riba*-based elements within a company's statements of financial position, must be less than 33 per cent.

(Extract from Securities Commission Malaysia, 2017)

Malaysia could be said as in the forefront in providing Islamic Capital Market instruments not just limited to the local but also to global players in fact Bursa Malaysia has won three prestigious award on Islamic capital market: The prestigious *Best Islamic Exchange 2016* conferred by Global Islamic Finance, *Best Islamic Exchange Asia 2016* and *Best Islamic Finance Facilitation Platform Asia 2016* by Global Banking and Finance Review and *Best Interbroker for Islamic Transactions 2016* at the 11th IFN Service Providers Poll 2016 for the outstanding performance of BSAS as a global commodity Murabahah trading platform (Bursa, 2016). By end 2015, Malaysia's ICM reached a size of RM1.7 trillion and accounted for 60.1% of the total size of the Malaysian capital market.(Securities Commission Malaysia, 2017).

The table 2 shows the progress of Islamic capital market from year 2012 to 2016 managed by Bursa Malaysia

Table 2: Islamic Capital Market development from 2012 to 2016

Islamic Capital Market	2012	2013	2014	2015	2016
% of Shariah Compliant PLCs	88	71	74	74	74
% of Shariah Compliant (by Market Capitalisation)					
• PLCs	64	63	63	66	64
• ETFs	32	30	31	21	22
• REITs	14	43	42	43	42
No. of ETBS	-	2	3	3	3
No. of Sukuk Listings on Bursa Malaysia Securities	20	20	20	22	24
Value of Sukuk Listings (USD billion)	33.7	32.9	34.2	34.6	53.5

Bursa Suq Al-Sila':					
• Average Daily Value Commodity Traded (RM Billion)	2.3	3.9	6.9	15.2	16.3
• Total Accumulated Commodity Trade Value (RM Billion)	563.3	958.9	1687.9	3727.7	3997.7
• Total No. of Matched Contracts	20858	285547	316534	350801	218087
• No. of Trading Days	245	247	246	246	246
• No. of BSAS Registered Participants:					
Total	69	78	93	109	124
- Domestic	51	60	73	87	98
- Foreign	18	18	20	22	26

(Extract from Market highlight, page 46, Bursa, 2016)

Table 2 clearly shows that the Islamic Unit trusts could only invest in 74 percent from the total companies available in Bursa Malaysia. Even though the percentage is quite high but it only accounted 64 percent from total market capitalisation. Therefore this study intends to investigate whether the deprive of highly valuable non shariah compliance companies to invest has translate into constraints in equity selections which in turn will lower their return as compare to their conventional counterparts.

Literature Review

Table 3 below is a summary of some related literature.

Table 3: Summary of Literature

Author/s	Sample and Method	findings
(Norma, Shabri Abd. Majid, Kassim, Hamid, & Yusof, 2010)	27-unit trust Malaysia, with five Islamic 2002-2005	efficiency of the Islamic unit trust companies is found to be comparable to their conventional counterparts
(Faleh, 2013)	52 Islamic equity funds, 63 ethical equity funds and 100 conventional equity funds, 2004 -2009	In general, Islamic funds have largely underperformed conventional funds. In the bearish period, the Islamic mutual fund outperformed the MSCI AC WORLD Index and the conventional mutual funds. During the bullish period, the conventional mutual funds outperformed the Islamic mutual funds.
(Hassan, 2003)	Islamic Screened stocks (based on Dow Jones Islamic Index 1996-2003	Expected returns of Islamic screened Portfolios are higher than the expected returns of conventional portfolios
(Alkassim, 2008)	13 global unit trust and 15 Malaysian Local funds 2000 -2006	Islamic unit trust is underperformed in terms of stock selection ability There is also evidence on negative performance persistence of Islamic unit trust
(Suhana, Raja Zuraidah, Nooririnah, Ruziah, & Zaibedah, 2012)	4 Islamic unit trust funds and 4 conventional unit trust funds 2005 - 2009	Islamic unit trust underperformed the KLCI
(Kassim & Kamil, 2012)	Malaysian Islamic Unit Trust 2000-2009	During the non-crisis economic period, the performance of the Islamic unit trusts is comparable to that of the market benchmark, During the economic crisis period, the Islamic unit trusts perform better compared to the non-crisis period.

(Ahmad & Haron, 2006)	12 Islamic funds and 77 conventional, Malaysian 2000-2003	Islamic funds failed to outperform the performance of conventional fund. However, the Islamic funds seemed to have lower risks than the conventional funds
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In summary, the results of the literature could be said as mix between outperformed (Hassan, 2003; Norma et al., 2010) and underperformed (Ahmad & Haron, 2006; Alkassim, 2008; Suhana et al., 2012). What is more interesting is where Faleh (2013) found that during the bearish period, Islamic unit trust is able to absorb the economic pressure better than their conventional counterparts.

Methodology

The data for this study is extract from the Thomson Reuters Eikon database by focusing on Malaysian unit trust products investing in Equity market at Bursa Malaysia. The database produce 108-unit trust products, however 9 of the products has been rejected as sample as it exists less than 5 years. Thus, the final sample is 99 unit trusts products where 46 of it are Islamic and the remaining 53 are conventional funds.

There are five performance measurement has been selected to test the differences namely; percentage of growth, risk reward, Sharpe, Treynor and Tracking error. All the performance measurement is based on five years performance.

Findings

Table 3 shows the result of comparing means by using two independent samples t test method.

Table 3: Two Independent samples t test for Comparing Performance of Islamic with Conventional Unit trust

Performance Measurement	Mean	SD	Mean Difference	T value	P Value
% growth i	34.77	19.851	-9.342	-2.005	.048
% growth c	44.12	25.621			
Risk/reward i	.2054	.08347	-.03928	-2.298	.024
Risk/reward c	.2447	.08599			
Sharpe i	.0848	.06174	-.03088	-2.096	.039
Sharpe c	.1157	.08168			
Treynor i	.2076	.15539	-.07635	-2.057	.042
Treynor c	.2840	.20597			
Tracking error i	1.1522	.46480	-.06556	-.601	.549
Tracking error c	1.2177	.59969			

The result shows that there are statistically significant mean difference between the mean percentage in Unit Trust performance between Islamic and conventional on percentage growth, risk/reward, Sharpe and Treynor as the p-value 0.048, 0.024, 0.039, 0.042 respectively are less than 0.05 significant value. Moreover, all these performance measurements also indicate that conventional unit trust are able to outperforms their Islamic counterparts as the mean value of conventional performance measurements are higher than the Islamic.

However, for Tracking error, the table shows that the t-test is not significant ($t = -.601$; $p = 0.549$) since p-value greater than 0.05 significant level, indicating that the tracking error 5 years are not significantly different between Islamic and conventional Unit Trusts.

The table 4 shows top 5 ranking unit trust products under the Sharpe and Treynor measurement.

Table 4: Top 10 Ranking based on Sharpe and Treynor

Ranking	Sharpe		Treynor	
	Islamic	Conventional	Islamic	Conventional
1	Eastspring Investments Dana al-Ilham	Kenanga Growth	PMB Shariah Aggressive	Kenanga Growth
2	PMB Shariah Aggressive	Eastspring Investments MY Focus	Eastspring Investments Dana al-Ilham	Eastspring Investments MY Focus
3	PMB Shariah Premier	Areca equityTrust	PMB Shariah Premier	Areca equityTrust
4	PMB Shariah Growth	Kenanga Malaysian Inc	PMB Shariah Growth	Saham Amanah Sabah
5	CIMB Islamic Equity Aggressive	Hong Leong Penny Stock	CIMB Islamic Equity Aggressive	Hong Leong Penny Stock
6	Kenanga Syariah Growth	AmMalaysia Equity	Kenanga Syariah Growth	Kenanga Malaysian Inc
7	Hong Leong Dana Makmur	Phillip Master Equity Growth	Hong Leong Dana Makmur	Phillip Master Equity Growth
8	AmIslamic Growth	Saham Amanah Sabah	Public Ittikal Sequel	AmMalaysia Equity
9	Public Ittikal Sequel	Eastspring Investments Growth	AmIslamic Growth	Eastspring Investments Growth
10	CIMB Islamic Al-Azzam Equity	PB Growth	MIDF Amanah Islamic	KSC Incrementum

For Islamic unit trusts, 9 products are rank consistently top 10 for both performance measurements. However, CIMB Islamic Al-Azzam Equity which ranks number 10 under Sharpe has been replaced with MIDF Amanah Islamic under Treynor. The same scenario also happened for conventional where PB growth, rank number 10 under Sharpe has been replaced by KSC Incrementum under Treynor.

Conclusion

The results of the study is consistent with Ahmad and Haron (2006), Alkassim, (2008) and Suhana et al. (2012) where Islamic Unit trust failed to outperform their conventional counterparts. However, this results should be read with cautious as it only cover for a medium period only. Results may be different under different economic scenario or different investment time frame. In addition to that, future research should investigate which factors contribute more to this results, is it managers skills or limitation of equities to select.

It is estimated about US\$9.5 trillion of global of Muslims wealth is intermediated by conventional financial institutions which could be tap by various parties in Islamic capital market (Securities Commission Malaysia, 2017). Thus, there are vast opportunities for the Islamic unit trust companies to tap. But they should prove that they are able to compete if not better than their conventional counterparts.

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