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Beyond Profit:

How Islamic Social Finance is Changing Lives and Empowering Humanity



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Introduction

Islamic finance, with its core principles rooted in Islamic law (Shariah), offers a unique approach to financial transactions. It prioritizes ethical conduct, social responsibility, and shared prosperity, aiming to create a just and equitable financial system. This focus on ethical principles positions Islamic finance as a powerful tool for changing lives and empowering humanity.

Malaysia has emerged as a global leader in Islamic finance, boasting a dynamic ecosystem that fosters not just financial growth but also social well-being. This leadership extends to Islamic social finance (ISF), a unique set of tools and practices that combine Islamic principles with social development goals.

The Emergence of Islamic Social Finance

The ISF instruments have a rich history in Malaysia. Zakat, the mandatory annual charity, has been a cornerstone of Islamic social welfare for centuries (Muhamat et al, 2013). Similarly, waqf (endowment) has played a vital role in financing mosques, schools, and hospitals for generations.

Malaysia has witnessed a surge in innovative ISF approaches. Islamic microfinance institutions like SME Bank and Bank Rakyat offer Shariah-compliant financing to entrepreneurs, empowering them to build businesses and create jobs. Sukuk, or colloquially

termed as Islamic bonds, have been structured to finance social impact projects like affordable housing and infrastructure development in underserved communities. This focus on social good aligns with Malaysia's aspirations as outlined in its national development plans such as the Twelfth Malaysian Plan (12MP).

The source of funding for Islamic social finance can be derived from two main contributors which are stream of income in the form of charity instrument such as zakat, donation, endowment or stream of income from instrument that require repayment, for instance sukuk, microfinancing and others.

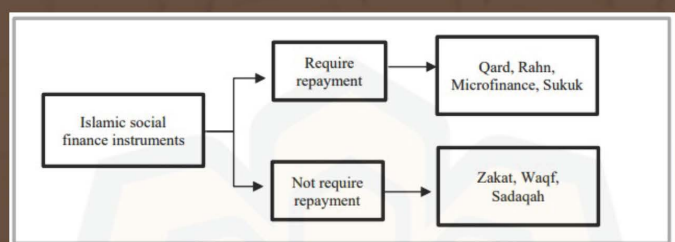


Diagram 1: Types of Islamic social finance instruments
Adapted from Rosman, Redzuan, Mokhtar, Ali & Mohammed (2022)

The Impact of ISF in Malaysia

The impact of ISF in Malaysia is undeniable. It fosters financial inclusion by providing access to financial services for underserved communities. By supporting microenterprises and entrepreneurs, ISF fuels economic growth and job creation. Furthermore, ISF contributes to social justice by channeling resources towards education, healthcare, and infrastructure development, particularly in underprivileged areas. This focus on social good strengthens societal well-being and promotes a more inclusive development model. Traditional finance can often exclude those deemed high-risk or lacking collateral which cause them to be the underserved population.

One example of the positive impact of Islamic social finance in Malaysia is a customised sukuk that has been developed for social finance and winning various awards such as Overall Deal of the Year 2020, Most Innovative Deal of the Year 2020 and Malaysia Deal of the Year 2020 by Islamic Finance News and Best Digital Sukuk at the 14th Annual Best Deal/Solution Awards 2020 by Alpha Southeast Asia was Sukuk Prihatin Malaysia.

The Sukuk Prihatin was a special-purpose, short-term Islamic bond issued by the Malaysian government in September 2020. The aimed was to raise funds specifically to combat the economic and social impacts of the COVID-19 pandemic. The Sukuk Prihatin reached maturity in September 2022 and was successfully redeemed by the government (Aziz, 2022). It set a precedent for socially driven Islamic bonds and highlighted how Islamic finance can be harnessed to address urgent societal needs (Kamarul Bahrin et al, 2024).

While ISF has continuously brought positive impact to the society but the benefits are noticeable by many during the pre and post pandemic COVID-19 period circa 2020-2022 which the ISF instruments were used extensively to assist the population and to revive the economy. Funds from zakat was used to assist not only the *asnaf* but also the larger population including the non-Muslims impacted by hardship of the dire situation. In the early months when COVID-19 hit Malaysia, the zakat authorities have started to disburse the zakat funds for various needs from foods to medical equipment for the frontliners and others (Muhamat, 2020).

Challenges and the Road Ahead

A significant portion of the Malaysian population, particularly those unfamiliar with Islamic finance concepts, may have limited understanding of ISF offerings. This lack of awareness can hinder broader adoption and utilization. Efforts to raise public awareness through educational programs and financial literacy initiatives are crucial to bridge this knowledge gap and empower potential beneficiaries (Kuanova, Sagiveya & Shirazi, 2021).

Striking a balance between fostering innovation in ISF products and maintaining a robust regulatory framework to ensure financial stability and consumer protection remains a challenge. Clear and comprehensive regulatory frameworks specifically tailored to ISF can provide a more conducive environment for the sector's growth.

The ISF sector requires a skilled workforce with expertise in both Islamic finance principles and social development practices. Building capacity through targeted training programs is essential. Establishing standardized metrics to effectively measure the social impact of ISF initiatives is crucial for demonstrating their effectiveness and attracting further investment (Widiastuti et al, 2022).

Conclusion

By prioritizing ethical conduct, social responsibility, and shared prosperity, Islamic finance offers a compelling alternative to traditional financial systems. Its focus on financial inclusion, ethical investment, social justice, and financial literacy positions it as a powerful tool for changing lives and empowering humanity. As Islamic finance continues to evolve and address its challenges, its positive impact on individuals and societies worldwide is likely to grow.

Islamic social finance in Malaysia serves as a powerful example of how financial systems can be harnessed to promote social good and empower individuals. By fostering financial inclusion, supporting social development, and promoting ethical finance, ISF is paving the way for a more just and equitable future for all Malaysians. This focus on social impact positions Malaysia as a leader in the global ISF landscape, inspiring and influencing the development of innovative solutions worldwide. As ISF continues to evolve in Malaysia, its positive impact on the lives of its citizens is certain to grow. Future research ought to explore on the innovative instruments to support the growth of this industry.

Despite identified challenges, Malaysia's Islamic social finance sector presents a compelling model for sustainable and inclusive development. Through collaborative efforts, Malaysia can solidify its position as a global leader in ISF and pave the way for a more equitable and prosperous future.



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