Vol. 3 No.1 pp. 110 - 123 | OCTOBER 2020
E-ISSN: 2735-1742
www.insla.usim.edu.my

EMBRACING VALUE-BASED REGULATION TOWARDS SUSTAINABILITY OF THE ISLAMIC FINANCIAL SYSTEM

Wan Norazimin Kassim & *Ruzian Markom

Faculty of Law, Universiti Kebangsaan Malaysia

*(Corresponding author) email: ruzian@ukm.edu.my

ABSTRACT

The legal and regulatory aspects of the Islamic financial system serve as the underlying catalyst of its sustainable development. Revitalizing good governance to achieve Shariah goal is the paramount consideration in the modern Islamic finance other than products development that offers a wide range of wholesale, retail, and trade financing solutions. The value-based intermediation initiative is the vehicle to transform the industry, from profitability and Shariah compliance to impactful services. After more than 30 years of its growth in Malaysia, this study will investigate the value-based regulations applied as a benchmark in the global Islamic finance industry. This study adopts a qualitative method which is mainly library research by analyzing the relevant works of literature on the subject and data from journal articles, websites, and official reports of the regulators. The study evaluates the legal and Shariah governance frameworks, existing practice, and measures in ensuring effective implementation of Islamic financial system considering the current issues and legal constraints. Findings of this study revealed that Malaysia has a set of value-based regulations, which also lead other countries. Hence, the study suggests that value-based regulations will contribute to the sustainability of the Malaysian Islamic financial system.

Keywords: *value-based, regulation, impactful service, sustainability, Islamic financial system.*

Introduction

The Islamic Financial Services Act 2013 (IFSA 2013) is the legal foundation of the modern development of the Islamic financial system in Malaysia. To support the socio-economic development, various programmes were introduced as value-based for Islamic finance industry globally, in line with the country's aspirations as the global Islamic finance hub. Towards this end, Malaysia's Islamic financial institutions are leading the sustainability agenda and spearheading sustainable finance through the adoption of value-based intermediation (VBI) initiatives. Of importance, VBI is the vehicle to transform the industry, from profitability and Shariah compliance to impactful services (The Central Bank of Malaysia, 2019). Through VBI, it is expected that Islamic finance will put the hand in hand various stakeholders to advance the sustainability agenda, encouraging Islamic financial institutions to assess how they create value and impact, particularly in response to dynamic circumstances of the world's economic, social and environmental conditions. Malaysia has taken a pragmatic approach in implementing VBI via industry-driven efforts, factoring in the different levels of readiness and capacity of individual Islamic banks to initiate and sustain the adoption of new business models and internal practices that are consistent with VBI (Bank Negara Financial Stability and Payment Systems Report, 2017). Creating the most conducive environment for Islamic financial system to thrive during the current economic instability period and post-pandemic COVID-19 is becoming more challenging. Equally important is the need to ensure Islamic finance can distinguish itself from conventional counterparts and optimize its unique characteristics to contribute to the sustainable development of the nation and globally. As Malaysia continues to demonstrate progressive development of public policies underpinned by the facilitative environment for the Islamic financial system, a study on this area with some consideration on international value-based will benefit towards enriching the knowledge and experience for further advancement of Islamic finance as a whole. Hence, the study explains the legal and Shariah governance framework of the Islamic finance in Malaysia and demonstrates the existing value-based regulations to effective implementation of Islamic financial system considering the current issues and legal constraints surrounding it. Also, it suggests embracing the value-based of the regulations towards sustainability of the Islamic financial system.

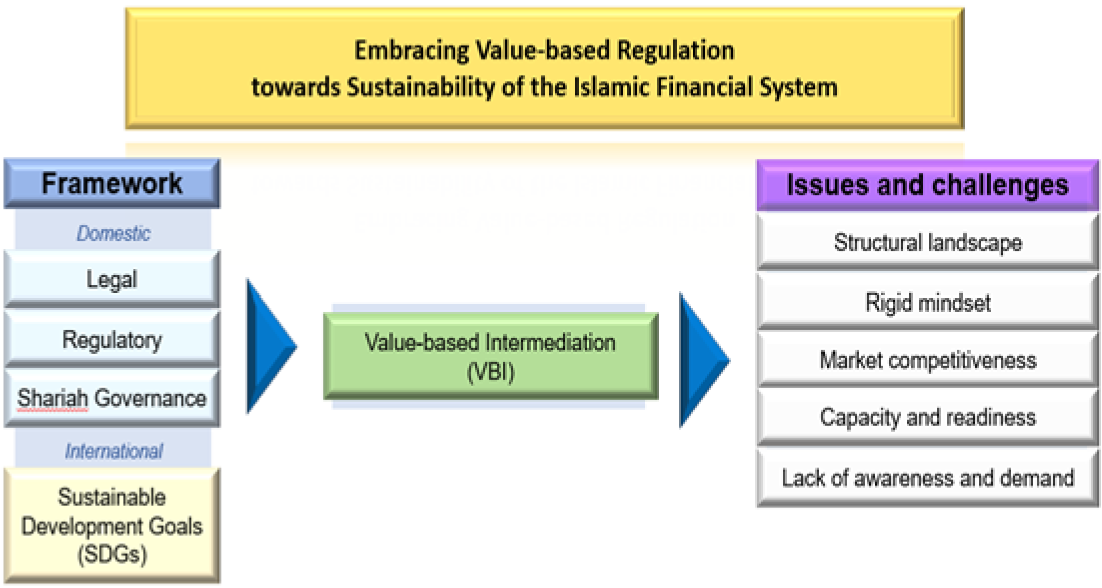

Diagram 1: Synopsis of study

Methodology

This is doctrinal research utilized content analysis in which the data obtained is from primary and secondary sources. The main sources of this research are the Islamic Financial Services Act 2013, the Value-based Intermediation Financing and Investment Impact Assessment Framework (VBIAF), the Implementation Guide for Value-based Intermediation, the Value-based Intermediation Scorecard and the Financial Stability and Payment Systems Reports of Bank Negara Malaysia issued from 2013 to 2019. The secondary sources referred to are journal articles, textbooks, case reports, policy documents and related documents. This study involves collecting information through library research. Each document is categorized according to priority in qualitative research in a non-doctrinal nature. The documents obtained are studied by category of documents and their application by legal principles.

Literature Review

Shariah Governance

Shariah governance is a key in the development of Islamic Financial System. The Malaysian model of the Shariah Governance Framework (SGF) is unique and could be emulated and adapted by other countries when developing the Islamic finance industry in their respective jurisdictions (Akram, 2018). According to reports, the emulation of the Malaysian SGF model is already under consideration by countries such as Bahrain, Pakistan and the UAE (Parker, 2017). The SGF is regarded as a controlling system to safeguard the Islamic Financial Institutions (IFIs) while governance practices that comply with Shariah guidance are essential for the sustainability of the Islamic banking industry (Rosli et.al, 2019).

Value-based Intermediation

VBI is defined as an intermediation function that aims to deliver the intended outcomes of Shariah through practices, conduct and offerings that generate positive and sustainable impact to the economy, community and environment, consistent with the shareholders' sustainable returns and long-term interests (Azren et. al, 2018). It is said that in Malaysia, the Islamic finance industry is well supported by comprehensive market infrastructure, robust regulatory framework and dynamic market participants as the industry's key growth drivers. Hence, moving forward, Malaysia must move the Islamic financial industry to the next level of growth that is sustainable, with a clear value proposition. Further, adoption of VBI initiative in the end-to-end operation of an institution also cultivates good and ethical conduct of the business operation. Customers then will receive better quality services from the provider. So, it was proposed that there are four underpinning thrusts of VBI that serve as preliminary guidance, that is, entrepreneurial mindset, community empowerment, good self-governance and best conduct.

Sustainable banking

Sustainable banking practices are pursued to ensure not only that banking processes minimally impact the environment but also that banking products and services become more environmentally friendly (Sherin et.al, 2018). According to the United Nations Documents (, sustainable indicates development that meets the needs of the present without compromising the ability of future generations to meet their own needs. Studies have shown that the approach and action taken by Islamic banks in Malaysia towards sustainability is not uniform. The strategic paper issued by the BNM in 2018 includes environment as one of the many objectives of an Islamic bank, however, the focus of value-based intermediation seems to be good governance (Sherin et.al, 2018).

Nur Farhah et. al (2019) considered three strategies by the Central Bank of Malaysia in the practical implementation of VBI are, rethinking value where the real value may be derived from the holistic objectives of Shariah, rethinking risk where the financial market and management's view of risks is reflecting sustainability factors, and changing the mindset to push the limits for IFSI in reaching holistic objectives of Shariah and sustainability. According to them, when VBI is mentioned, it gives a focus on the financial intermediary role of Islamic financial institutions in delivering positive and sustainable impacts on the society, SDGs specifically focus on the set goals and their achievements. Islamic social finance and its instruments are important tools for the success of VBI and essential for the sustainability of IFSI (Nur Farhah et. al,2019). Hence, this study demonstrates whether contracts that are based on social finance are preferable in the implementation of VBI since it is Shariah-compliant and making SDGs as counterparts.

Since the positive impact of Islamic financial instruments worldwide, this study examines the position of Malaysia as an example of embracing value-based regulations. It is imperative to note that Malaysia, Bahrain, and the UAE remained the top markets in terms of Islamic finance development. Malaysia is a strong leader in terms of indicator value, sitting in pole position for all indicators other than CSR (ICD-Refinitiv Islamic Finance Development Report, 2019).

Diagram 2: Top 10 Islamic Finance Development Indicator (IFDI) Markets 2019

		Ranking					
Country	IFDI Value	IFDI 2019	Quantitative Development	Knowledge	Governance	CSR	Awareness
Malaysia	115	1	1	1	1	11	1
Bahrain	71	2	4	6	2	7	3
United Arab Emirates	70	3	6	5	3	6	2
Indonesia	68	4	8	2	9	13	10
Saudi Arabia	60	5	5	8	20	2	7
Jordan	57	6	17	4	13	1	13
Pakistan	56	7	13	3	7	17	4
Kuwait	54	8	2	22	8	4	9
Oman	52	9	12	11	4	3	8
Brunei Darussalam	45	10	19	7	5	24	5

Source: ICD-Refinitiv Islamic Finance Development Report, 2019

Findings of the Study

The Overview of Legal and Shariah Governance Framework for Malaysian Islamic Finance

Historically, Malaysia's Law Harmonisation Committee was formed in 2010 to identify and make recommendations for creating a more conducive legal system to facilitate the development of Islamic finance in Malaysia. Throughout the evolution, Malaysia has developed a comprehensive and sophisticated Islamic finance marketplace that has grown from strength to strength for over 30 years since the enactment of the Islamic Banking Act 1983 (The Central Bank of Malaysia, 2014).

Bank Islam Malaysia Berhad was established as the first fully-fledged bank that offered Islamic banking products and services way back in 1983 (Sherin, 2012). This was due to the introduction of the Islamic Banking Act 1983 and the Takaful Act 1984 which were remarkable statutes in the global Islamic financial system. Further to strengthen its development in 1993, commercial banks, merchant banks and finance companies could offer Islamic banking products and services under what was known as Islamic banking scheme also known as "Islamic windows".

Malaysia then has a turning point when in January 1994, for the Islamic banking system to function as a full-fledged banking system, an Islamic Interbank Money Market (IIMM) was set up, to link the institutions and the instruments (Sherin, 2012). This was followed by the establishment of a National Shariah Advisory Council under the auspices of the Central Bank of Malaysia Act 1957 which statutory function is to advise the Central Bank of Malaysia on Islamic banking operations. Generally, its role is to ensure overall coherence to principals of Islam and that all banks offering Islamic services conform to the same principals. The scope, mandate, and binding nature of Shariah Advisory Council's resolutions in the context of Islamic financial system have been further reinforced through the enactment of Central Bank of Malaysia Act 2009.

Later in 2013, the Islamic Financial Services Act 2013 (IFSA 2013) was enacted to catalyse modernization of Islamic financial system in Malaysia based on its unique value propositions. IFSA 2013 provides the statutory foundation for a Shariah contracts-based regulatory framework in a manner that would facilitate the next level of Islamic banking business, transcending beyond financial intermediation to include real economic sector participation, complete with the consequent regulatory checks and balances, thereby increasing the level of transparency required (The Central Bank of Malaysia, 2014).

To note, Malaysia has a comprehensive suite of Islamic financial products and services both onshore and offshore. The Labuan Islamic Financial Services and Securities Act 2010 streamlines procedures and requirements of all Shariah-related activities conducted in Labuan IBFC, including protected cell companies, limited partnerships and limited liability partnerships, private trust companies, trusts and foundations to broaden the pool of Shariah-compliant wealth management tools (The Central bank of Malaysia, 2014).

The Islamic capital market in Malaysia has become an integral component of the mainstream financial system. As a marketplace for global Sukuk, Malaysia issued USD58 billion, or 70% of total global Sukuk of USD83 billion for the first 3 quarters of 2013 (The Central Bank of Malaysia, 2014). Islamic equity market products in Malaysia include Shariah-compliant equities, Shariah-compliant collective investment schemes (unit trust funds, wholesale funds, I-REITs, I-ETFs), structured products, alternative funds (real estate, leasing, commodities), private equity funds and mixed asset (equity + fixed income + cash). An I-REIT is a collective investment scheme that invests in a portfolio of income-generating properties in which the tenants operate permissible activities according to Shariah. Rents collected from tenants, fewer expenses, are distributed regularly to provide stable yields to unitholders. I-ETFs are listed open-ended funds that track an Islamic benchmark index whereby the constituents are Shariah-compliant companies.

The financial system in Malaysia is well supported by the required financial infrastructure. The introduction of the first electronic multicurrency commodity trading platform, Bursa Suq Al-Sila' facilitates financing for Islamic financial institutions and liquidity management (The Central Bank of Malaysia, 2014). Thus, Islamic financial institutions are required to have in place appropriate policies and procedures to manage exposures to commodity trading risks in line with the policy documents (PDs) issued by the Central Bank on Murabahah and Tawarruq (The Central Bank of Malaysia, 2019).

According to the enactment of IFSA 2013, it was projected that the evolution of a comprehensive mix of products based on primary and financing models is a major move which will significantly alter the current banking business model of Islamic banks (The Central Bank of Malaysia, 2013). The Investment Account Framework (IAF), introduced in 2014, supports investment intermediation by strengthening the entrepreneurial role of Islamic banks in optimising funds for productive uses in the economy, in which in response to the divergent practices observed in the operationalisation of investment account, the Central Bank of Malaysia provided additional guidance to the industry on its expectations around product structuring, operational management and business conduct in the offering of investment account. This is also supported by a subsequent review of the Shariah Governance Framework that was initiated by the Central Bank of Malaysia in the first quarter of 2016 to take into account the more mature Islamic banking and takaful industry that has evolved in Malaysia (The Central Bank of Malaysia, 2016).

The development of high-quality talent for Islamic finance remains a priority of the Central Bank of Malaysia whereby in November 2016, the Steering Committee for Transformation of the Education Landscape for Islamic Finance (Steering Committee) was formed to frame a clear industry-led strategic direction for talent service providers in Malaysia. The focus is on strengthening the Central Bank of Malaysia's affiliates, namely INCEIF, the International Shariah Research Academy (ISRA), the Islamic Banking and Finance Institute Malaysia (IBFIM), the Chartered Institute of Islamic Finance Professionals (CIIF) and the Association of Shariah Advisors (ASAS) (The Central Bank of Malaysia, 2016). The Central Bank of Malaysia also developed the first dedicated training programmes for Shariah personnel and the top management in Islamic banks, as well as the first Educator's Manual on Shariah Standards and Operational Requirements in the same year.

The Concept of Sustainability in Islamic Finance

Value-based Projects, Products and Services

To expand the impact on value chains, more needs to be done for certain sustainable development goals (SDGs), especially SDG #7: Affordable Energy, SDG #8: Decent Work and Economic Growth, and SDG #9: Industrial Innovation and Infrastructure Development (Ahmet Suayb Gundogdu, 2018). He regarded that to assure the allocation of resources and work effort to viable and value-adding projects, the market mark-up rate should be used for project proposals related to these three SDGs. A major characteristic of an Islamic financial system that enables it to uniquely contribute to economic growth process is the profit-sharing principle, which foster equity in income distribution leading to social justice and long-term economic growth (Salina, 2016). She referred to a theoretical study conducted by Nagaoka in 2011 that Islamic finance is found to embed the monetary sector into the real sector (embedded financial system), which is described as a universal financial system characterised by a great potential of sustainable development. Also, a comparison study by Yusof and Bahlous in 2013 between Gulf Cooperation Council (GCC) and Malaysia and Indonesia, using annual data over the period 2000 to 2009 and employing panel cointegration, variance decompositions and impulse response functions, the study finds that Islamic banking contributes to the growth process of these countries, both in the short and long runs, but contribution in Malaysia and Indonesia is stronger, in the short runs, rather than the GCC Countries. The results of her study revealed that while the Islamic deposits are not having significant effect on the real economy in the short run, in the long run, the Islamic deposits are having a positive effect on the real economy. In this regard, the study suggests that Islamic banks should promote Shariah-compliant investment deposits to attract long-term savers and avoid the time lag in pooling funds for investment purposes.

Notably, the Shariah Advisory Council of the Central Bank of Malaysia (SAC) has produced several path breaking Shariah rulings which have not only instilled customer and market confidence but have also catalysed several industry innovations. Two rulings in the year 2018, one is SAC's endorsement of the application of al-ijarah thumma al-bai` (leasing followed by sale), for example, has allowed the offering of more competitive vehicle financing solutions by more than 15 Islamic banking institutions. Another area is the ruling on the imposition of late payment charges by Islamic banks using gharamah (penalty) and ta`widh (compensation) which has allowed Islamic financial institutions to operate on a level playing field with their conventional counterparts (The Central Bank of Malaysia, 2018). It was observed that the Central Bank of Malaysia had published in its website a series of Shariah standards covering key Shariah contracts such as Murabahah, Musharakah, Mudharabah, Istisna', Ijarah and Tawarruq.

Some of the common ways an Islamic bank conducts its business is through either buying or selling of goods, in cash and/or in credit for a profit as in Murabahah; or through equity participation by partnerships such as Musharakah or Mudarabah; or through leasing of items and obtaining rentals such as in ijarah (Sherin, 2012). Islamic banks can also charge fees for their services as in Juala or Ujr or act as an agent (Wakalah) and obtain a fee from there. Sherin (2012) also suggested, based on her finding from RHB Bank's website that the practice of awarding Hibah to depositors is deemed necessary as the Islamic banking system in Malaysia operates parallel to commercial banks (known as a dual system) and therefore, needs to be competitive in the banking environment.

The main contracts that are commonly used are Mudharabah, Murabahah, Musharakah, Ijarah and Wakalah. Prudential standards and applicable market practices for Islamic financial institutions are in line with global standards and value based (The Central Bank of Malaysia, 2016). For instance, Deposit-Taking under Mudharabah Contract is a partnership contract where the depositor provides the capital and the Islamic bank plays the roles of both manager and entrepreneur (The Central Bank of Malaysia, 2014). In particular, the most used models in takaful are agent-principal (Wakalah) and profit sharing (Mudharabah) (The Central Bank of Malaysia, 2014). On the other hand, commonly used principles to structure Sukuk are contract of exchange such as Ijarah, Murabahah and Istisna', and contract of participation such as Musharakah and Mudharabah.

Consistent with Shariah principles, the adoption of value-based intermediation (VBI) will further sharpen the focus of Islamic financial institutions in ensuring their products, services and practices deliver a positive and sustainable impact on the economy, community and environment (The Central Bank of Malaysia, 2018). In the capital market sphere, Sukuk had served as an alternative form of financing for businesses, with the thrive of innovation such as green Sukuk for green businesses. To date, five green Sukuk have been issued by Malaysian solar companies to finance solar power projects, amounting to RM866.8 million since July 2017 (The Central Bank of Malaysia, 2019).

Currently, VBI is one of the relevant developments that taking place under the sustainable agenda. In 2016, the Central Bank of Malaysia drove and supported many initiatives to encourage a stronger focus on VBI as a core premise for Islamic financial solutions and to facilitate greater innovation in Islamic product offerings (The Central Bank of Malaysia, 2016). This is developed when Islamic banking products have evolved from basic consumer or retail products into a full range of product offerings (e.g. corporate, project financing and long-term bond instruments) under various Islamic contracts (The Central Bank of Malaysia, 2014).

VBI aims to deliver the intended outcomes of Shariah through practices, conduct and offerings that generate positive and sustainable impact to the economy, community, and environment, without compromising on the financial returns to shareholders (Mohamad Rafique, 2017). As at its inception, nine Islamic banking institutions namely Bank Islam, Bank Muamalat, ClMB Islamic, Agrobank, HSBC Amanah, Maybank Islamic, AmBank Islamic, Alliance Islamic and Standard Chartered Saadiq have formed the VBI Community of Practitioner.

After the financial crisis, many developed and developing countries such as Malaysia, had issued guidelines on corporate governance as best practices code (Ummi Sulaim et. al, 2018). It is worth to note here that in cases of conflict between stability and consumer protection, priority was given to stability, which was often equated with the profitability of financial institutions (Islamic Financial Services Board, 2015). Hence, development of new products featuring key elements of VBI and diversified Shariah contracts has been one of the potent tools and key driver to enhance competitiveness and sustainability of Islamic financial system while opening up opportunities to integrate Malaysia with the global economic and financial market.

Making VBI the Value-based Regulation

Since November 2019, a framework for VBI namely VBI Financing and Investment Impact Assessment Framework (VBIAF) was introduced by the Central Bank of Malaysia. It outlines the framework to facilitate the establishment of an effective risk management system for financing and related advisory services and investment activities that integrate the VBI. With the principles of VBIAF, the purpose of VBI implementation is more strategic and guided through. VBIAF suggests eight key principles to be adopted by Islamic financial institutions, together with illustrations and examples of value-based across the globe. Noting that the World Bank Group (Malaysia Office) and the International Centre for Education in Islamic Finance (INCEIF) has collaborated with the Central Bank of Malaysia in preparing the VBIAF, and the World Wide Fund for Nature (WWF) (Malaysia and Singapore Offices) also made a significant contribution towards its drafting more on the environment and social aspects, all guidance and further guidance are inclusive in detail, and that covering all aspects of VBI framework, that is portfolio and customer perspectives. But the scope discussed is based on the respective technical, operational and financial VBI implementation strategy of individual Islamic financial institutions, which may differ according to risk appetite, capacity and capabilities.

Since the adoption of VBI strategy is voluntary, reference is also made to the Implementation Guide for VBI (2018) which intended to facilitate the adoption of VBI by Islamic banking institutions (IBIs) through three key aspects including sharing of practical banking practices that are driven by impact creation to wide stakeholders and deliberating key implementation challenges and issues as well as pragmatic solutions. Those three aspects help this study very much towards concluding the key findings of this Article.

Issues and Challenges towards Sustainable Islamic Financial System

Malaysia has been on the right track in advancing an ecosystem that supports the sustainable development of Islamic finance. It is important as well to ponder how the roles of Islamic finance would evolve against the new norms post-COVID-19 era. Islamic finance was initially introduced as an alternative mode of finance to serve the religious needs of the Muslim community, and eventually become a mainstream component of the financial system. However, it remains to be seen how Islamic finance can further establish distinctive branding and offer more unique propositions in serving the sustainable development agenda not only at the domestic market but also globally. Embracing value-based requires a holistic approach to be considered to substantially transform the entrenched practices within the finance industry. It is therefore important to understand key issues and challenges surrounding the Islamic finance industry itself.

a. The Structural Landscape of Islamic Finance is based on 'Leverage Model'

A review of the structural landscape of Islamic financial system in Malaysia reveals that the majority Islamic financial institutions are operating as a subsidiary of the conventional financial institutions, which is also known as a 'leverage model'. This explains that resource allocation and strategic direction of Islamic subsidiaries are subjected to the Group's policies, hence changes in business modality and internal capacity building are restricted (Central Bank of Malaysia, 2018). While the regulators have instituted a relatively advanced enabling legal and regulatory framework that caters for different business models, it can be deduced that the shareholders of Islamic banks and takaful operators seem to have a strong preference on adopting a leverage model – an approach that seemingly aims towards optimising operational efficiency, reducing overhead costs and ultimately maximising business profit.

b. The Issue of Rigid Mindset at Various Level of Decision-Making Authority

Such apparent conventional wisdom may have helped to maximise shareholder's values from a business viewpoint, but it is highly disadvantageous from a developmental perspective. It has led to the issue of rigid mindset at various levels of decision-making authority within Islamic financial institutions and prevent transformative ideas to unleash the real value propositions of Islamic finance from being implemented. As a result, products and services offered in the sphere of Islamic finance are mostly comparable to their conventional counterparts, using the underlying Shariah contracts as a conduit of product structure rather than the anchor of product innovation itself. Alternatively, impact-driven mindset may drive IBIs to explore and serve the underserved segment or new business opportunities such as SME and renewable energy (Central Bank of Malaysia, 2018). As Malaysia has various institutions offering Islamic finance courses – for both academic and professional qualifications – it is an utmost hope that the incoming new breed of talents with both Shariah-and business-savvy background will gradually steer the industry into a better position moving forward.

c. Market Competitiveness

Besides, market competitiveness is another key issue that should be considered in the implementation of impact-driven products. This is attributable to a longer turn-around-time required to approve financing or investment applications of such products which are not comparable to the traditional financial solutions. These non-traditional products are subjected to additional considerations in existing credit or investment appraisal. To gain more potential customers that adopt sustainable practices would require advisory and necessary knowledge on the principles of VBI, which also embrace the Shariah and legal principles.

Embracing changes also necessitate capacity and readiness within the industry to be put in place. These encapsulate the low uptake of products and services that embed distinctive features of Shariah contracts and VBI principles. Introducing products and services which do not conform to the typical financial products means changes have to be considered in many aspects including recalibration of the core banking system, re-training existing staff, adjusting the credit approval and risk management framework, ensuring the accuracy of marketing materials, as well as establishing new standard operating procedures (SOP) at all customers' touchpoints. These entail costly investment and longer time-to-market for new products, both are difficult considerations for those with decision-making authorities in the financial institutions.

d. Lack of Awareness and Demand for New Products and Services

Finally, addressing a lack of awareness and demand for new products and services that are unfamiliar to customers, especially post COVID-19 era, is an extra challenge for Islamic banks. As society readjusting themselves to the new norms and recover from economic challenges posed by COVID-19 situation, it is a question of priority that matters for most people. Surviving with the existing credit exposures and serving monthly payment obligation may be of the highest importance rather than searching for new financial products that generate positive impacts to the people and planet. Notwithstanding that, there are market segments with strong affiliation to these positive values and this potential individual, corporate and institutional customers are expected to increase over time.

Measures to ensure effective implementation of VBI regulation

a. VBI Impact Assessment Framework (VBIAF) and the VBI Scorecard

VBI Impact Assessment Framework (VBIAF) and the VBI Scorecard were launched for public consultation whereby, the Assessment Framework guides the assessment of financing and investment applications taking into consideration economic, social and environmental impacts, while the Scorecard supports the implementation of performance measurement frameworks for Islamic financial institutions that drive positive value and impact on society and the environment.

b. Waqf Fund Initiative

The Central Bank of Malaysia through the Association of Islamic Banking and Financial Institutions Malaysia (AIBIM) has called for Islamic Banks' participation in collaborating and standardising Waqf Fund initiative action plan, established as myWakaf (myWakaf, 2020). This initiative between Islamic Banks and State Islamic Religious Council under the Financial Sector Blueprint 2011-2020 is aimed at developing the potential of Waqf and empower the economy of ummah in Malaysia through a collaborative effort with Islamic banks.

c. Measurable KPIs – sustainability, ESG and good conduct management

According to the Implementation Guide of the VBI (2018), Islamic banking institutions (IBIs) are expected to identify measurable KPIs for each implementation strategies. Focusing on sustainability, ESG and good conduct management, illustrations are provided to facilitate the adoption of VBI through integration into key operational aspects, one of them is on products and services. IBIs who indicate a commitment to embrace VBI should reflect the adoption of value-based in product development, marketing, sales and product delivery and after-sales service, which aim to create more values to customers, as distinct features. Among the examples of banking practices highlighted by the Guide are the establishment of Product Research & Development Department/ Unit to generate product and infrastructure innovation ideas.

d. Empowerment Programs

A Program known as Program Keusahawanan Taylor's-CIMB Islamic is another community empowerment program that develops entrepreneurial abilities among B40 communities. It is said that strategic partnership with Taylor's Education Group enabled CIMB Islamic to leverage on the former's forte on teaching and education to complement the provision of financing solutions with non-financial services and also individual business coaching (Central Bank of Malaysia, 2018).

e. The proactive and inclusive structured engagement framework of multi-stakeholders

One good practice in another operational aspect of stakeholder management which aim to create a win-win situation for all is the proactive and inclusive structured engagement framework addressing interests of multi-stakeholders by Maybank. The engagement activities were conducted, while Maybank's response to any issues raised during the engagement sessions was documented and reported in its Sustainability Report considering key matters and meaningful conversation with both its internal and external stakeholders.

f. Financial Institutions stay focus on the implementation of VBI

In terms of the structural landscape issue, Islamic banking institutions should stay focus on a function that is currently controlled and managed by Islamic subsidiaries with a long-term view to create success stories as measures in VBI implementation (Central Bank of Malaysia, 2018). Upon delivering meaningful impacts from the VBI implementation, it is hoped that the success stories will induce realignment of other functions within the banking group towards conformity to principles of VBI and Shariah principles as well.

g. Financial Institutions provides literacy programs to existing and potential customers

From market competitiveness aspect, it is said that Islamic banks are expected to manage their business by nurturing existing and potential customers to adopt sustainable practices, instead of immediately exit from the transaction and by providing financial and non-financial solutions such as advisory that facilitate the customer to adopt sustainable practices (Central Bank of Malaysia, 2018). On capacity and readiness, adoption of VBI in business activities and banking practices must be proportionate with risk management capability and capacities while enhancement of capacity building involves the adoption of facilitative technology and leveraging on strategic partners' technical competencies and risk management infrastructure (Central Bank of Malaysia, 2018). From a legal point of view, compliance measures at each Islamic bank need to be strengthened and developed further to uphold the trust of the customers.

h. Financial Institutions Develop Targeted Awareness Program

In addressing the issue of lack of awareness and demand, concerted effort is required to develop a more targeted awareness program not only by each bank but also at the industry level. The Customer Satisfaction Index for Malaysia Banking Industry 2017 by Malaysian Productivity Corporation revealed that many banking customers are willing to pay extra for better service (Central Bank of Malaysia, 2018). Additionally, awareness programmes are indispensable since investors are increasingly expecting and demanding their investee companies to operate in a manner that generates a positive and sustainable impact on wider stakeholders.

Conclusion

The current new norms in the wake of post-COVID-19 economic recovery present great opportunities for Islamic finance to attain recognition as an important component of the mainstream financial system globally. It is time for Islamic finance to unleash its potential by upholding its unique value propositions and distinct characteristics while achieving the intended Maqasid Shariah. An integral part of this aspiration is to adopt more diversified Shariah contracts within product offerings and operational practices – in creating value-added impacts on the people, planet, and profitability of all interested parties and stakeholders. All Islamic financial institutions should recalibrate their existing products and services to be consistent with the key principles enshrined in the VBIAF and reposition themselves in securing their brand values in the eyes of customers and other stakeholders globally. From a regulation standpoint, it is noteworthy that Malaysia is on the right track in leading the value-based for industry's adoption towards cementing a more sustainable Islamic financial system under the new regime, the IFSA 2013. Given the appropriate and sufficient framework as well as value-based, public rights and interests are the paramount consideration in policymaking. Further in future, there is a need to enriching its literature and building greater public confidence through structured ways to improve industry practices, including those recommended under VBIAF as discussed above and explore how Islamic finance can further contribute to the more sustainable development of the nation and globally post COVID-19 era.

References

Ahmet Suayb Gundogdu. 2018. An Inquiry into Islamic Finance from the Perspective of Sustainable Development Goals. European Journal of Sustainable Development (2018), 7, 4, p. 381-390.

Azren Rizuani et al. 2018. Strategy Paper Value-based Intermediation: Strengthening the Roles and Impact of Islamic Finance https://www.bnm.gov.my/index.php?ch=57&pg=137&ac=612&bb=file. [29 June 2020].

Central Bank of Malaysia. 2013. Financial Stability and Payment System Report.

Central Bank of Malaysia. 2016. Financial Stability and Payment System Report.

Central Bank of Malaysia. 2017. Financial Stability and Payment System Report

Central Bank of Malaysia. 2018. Financial Stability and Payment System Report.

Central Bank of Malaysia. 2018. Assistant Governor's Speech at the IFN Green and Sustainable Finance Forum.https://www.bnm.gov.my/index.php?ch=en_speech&pg=en_speech&ac=810&lang=en Governor's Keynote Address at the Global Islamic Finance Forum 2018 (GIFF) - "Value Based Intermediation - Beyond Profit". [29 June 2020].

Central Bank of Malaysia. 2018. Implementation Guide for Value-based Intermediation.

Central Bank of Malaysia. 2019. https://www.bnm.gov.my/index.php?ch=en_speech&pg=en_speech&ac=819&lang=en. [29 June 2020].

Central Bank of Malaysia. 2019. Retrieved from https://www.bnm.gov.my/index.php?ch=en_speech&pg=en_speech&ac=845&lang=en. Assistant Governor's Speech at the IFN Green and Sustainable Finance Forum. [29 June 2020].

Central Bank of Malaysia. 2020. https://www.bnm.gov.my/index.php?ch=en_speech&pg=en_speech&ac=838&lang=en Deputy Governor’s Welcoming Remarks at the RFI Roundtable on Responsible Finance: "Unlocking Full Potential of Islamic Finance through Sustainability". [29 June 2020].

Central Bank of Malaysia. 2019. Financial Stability Review - Second Half 2019.

Central Bank of Malaysia. 2019. Value-based Intermediation Financing and Impact Assessment Framework.

Central Bank of Malaysia Act, 2009.

ICD Refinitiv. 2019. Islamic Finance Development Report 2019.

Islamic Financial Services Act 2013.

Islamic Financial Services Board. 2015. IFSB Working Paper Series Wp-03/10/2015ifsb Working Paper on Financial Consumer Protection in Islamic Finance.

Labuan Islamic Financial Services and Securities Act 2010.

Mohamad Akram Laldin. 2018. Islamic Financial Services Act (IFSA) 2013 and the Sharīʿah-compliance requirement of the Islamic finance industry in Malaysia. ISRA International Journal of Islamic Finance. Vol. 10 No.1, p. 94-101.

Mohamad Rafique Merican. 2017. Islamic Finance and Sustainable Economy. Hub Symposium. Edition 2017.

MyWakaf.com.my. 2020. [15 July 2020].

Nur Farhah Mahadi, Nor Razinah Mohd Zain & Engku Rabiah Adawiah Engku Ali. 2019. Leading Towards Impactful Islamic Social Finance: Malaysian Experience With The Value-Based Intermediation Approach. Al-Shajarah, Journal of Islamic Thought and Civilization of The International Islamic University Malaysia. Special Issue: Islamic Banking and Finance, p. 69-87.

Parker, M. (2017). “BNM’s Syariah Governance”, New Straits Times, 21 January, available at:

www.nst.com.my/opinion/columnists/2017/12/319043/bnms-syariahgovernance.[29 September 2020].

Rosli Abdul Aziz, Aisyah Abdul Rahman & Ruzian Markom. 2019. Best Practices for Internal Shariah Governance Framework: Lessons from Malaysian Islamic Banks. Asian Journal of Accounting and Governance 12, p. 37-49.

Salina Kassim. 2016. Islamic Finance and Economic Growth: The Malaysian Experience. Global Finance Journal (2016).

Sherin K. 2012. Islamic Banking in Malaysia. Internation Journal of Legal Information. International Association of Law Libraries. https://www.researchgate.net/publication/274961364. [30 June 2020].

Sherin K., Sarah YTL & M. Roslan. 2018. Sustainable Financing and Enhancing the Role of Islamic Banks in Malaysia. Arab Law Quarterly 32 (2018), p. 129-157.

Ummi Sulaim, Aisyah & Ruzian Markom. 2018. The Regulatory Framework on Liquidity Risk Management of Islamic Banking in Malaysia. International Journal of Business and Society, Vol.19 S3, 2018, p. 332-352.

United Nations. 1987. United Nations Documents, Report of the World Commission on Environment and Development: Our Common Future, Annex to Document A/42/427 (1987), available at www.un-documents.net/wced-ocf.htm. [19 September 2020].