THE ROLE OF CENTRAL BANK OF MALAYSIA IN POSITIONING MALAYSIA AS A GLOBAL HUB FOR ISLAMIC FINANCE

MOHD NAZRI BIN MOHD NOOR

ACADEMY OF ISLAMIC STUDIES
UNIVERSITY OF MALAYA
KUALA LUMPUR
2016

THE ROLE OF CENTRAL BANK OF MALAYSIA IN POSITIONING MALAYSIA AS A GLOBAL HUB FOR ISLAMIC FINANCE

MOHD NAZRI BIN MOHD NOOR

THESIS SUBMITTED IN FULFILLMENT OF THE REQUIREMENTS FOR THE DEGREE OF DOCTOR OF PHILOSOPHY

ACADEMY OF ISLAMIC STUDIES
UNIVERSITY OF MALAYA
KUALA LUMPUR

2016

ABSTRACT

This study examined the roles of the Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic finance. In investigating the roles, the meaning of the Islamic finance global hub was described and the development of a financial system until the formation of a global financial hub was examined. A study was conducted to determine the measures taken by the Central Bank of Malaysia as the sole financial regulator in strategizing plans and directions towards positioning Malaysia as an Islamic finance global hub. The findings show that among the measures taken include the drafting of the Financial Sector Master Plan, which aims to position Malaysia as a global Islamic financial center beginning from 2001 until the end of 2010. The second stage of the plan was designed from 2010 until 2020. The plan clearly defines the direction for Malaysia to emerge as a global Islamic financial hub. To further support this research, several interviews were conducted among a number of high-level representatives from the Department of Islamic Banking, Takaful of the Central Bank of Malaysia and the Islamic Financial Services Board and Islamic finance scholars. The purpose of the interview was to get clarification on the roles of the Central Bank of Malaysia in positioning Malaysia as an Islamic finance global hub. In addition, several questions regarding the positive and negative impacts from this policy were also raised. This study also applied a survey method in order to get respondents' view pertaining to the proposal of Islamic finance global hub index. Based on the findings of the study, some suggestions are presented which include proposals to develop a method to assess a global Islamic financial hub. This method is expected to serve as a guideline in evaluating a global Islamic financial center.

ABSTRAK

Kajian ini mengeksplorasi peranan Bank Negara Malaysia dalam menjadikan Malaysia sebagai sebuah hub kewangan Islam. Pada peringkat permulaan tesis ini menghuraikan pengertian hub kewangan Islam global dan meneliti peringkat perkembangan sebuah sistem kewangan sehingga terbentuknya hub kewangan global. Bank Negara Malaysia selaku bank pusat Malaysia telah merangka strategi dalam menjadikan negara ini sebagai sebuah hub kewangan Islam global. Antara langkah-langkah yang dijalankan termasuklah merangka Pelan Utama Sektor Kewangan yang mensasarkan Malaysia sebagai sebuah pusat kewangan Islam global bermula pada tahun 2001 dan berakhir pada 2010. Kemudian, peringkat kedua pelan tersebut dirangka bermula daripada tahun 2010 sehingga tahun 2020. Pelan ini dengan jelas menentukan halatuju Malaysia agar muncul sebagai hub kewangan Islam global. Bagi mengukuhkan lagi kajian ini, beberapa sesi temuduga dijalankan ke atas beberapa orang pegawai tinggi Bank Negara Malaysia daripada Jabatan Perbankan Islam dan Takaful. Tujuan temuduga adalah bagi mendapatkan pengesahan berhubung peranan Bank Negara Malaysia dalam menjadikan Malaysia sebuah hub kewangan Islam global. Beberapa soalan berhubung kesan positif dan negatif dari polisi ini juga ditimbulkan. Kajian lapangan juga telah dijalankan bagi menguji kerangka penilaian pusat kewangan Islam global. Kajian ini telah dianalisa menggunakan teknik diskriptif dan mean serta ditambah ulasan pakar dalam kewangan Islam. Di akhir kajian, beberapa cadangan dikemukan antaranya ialah cadangan bagi mengatasi halangan dan cabaran dalam proses membangunkan sebuah pusat kewangan Islam global di samping satu kerangka penilaian bagi menilai pusat kewangan Islam global. Kaedah ini diharap dapat dijadikan panduan dalam menilai sesebuah pusat kewangan Islam Global.

ACKNOWLEDGMENT

Praise be to Allah the almighty and the creator of the universe, and peace and blessings be upon the noble Prophet Muhammad Ṣ.A.W.

Alhamdulillah, thanks to Allah, the Almighty god who governs the nature which through His guidance and grace, this thesis could be completed. Special tribute dedicated to Prof. Dr. Joni Tamkin Bin Borhan, as a supervisor which by his consultancy and proper guidance leads to the completion of this study. A gratitude also dedicated to Dr. Patmawati Binti Haji Ibrahim, the former supervisor for her ideas and advices which favored in setting up the initial stage of this study.

The researcher also likes to address gratitude and congratulation to those individuals who are involve in giving ideas and insights to produce this study in a comprehensive form. Many thanks dedicated especially to former dean of Faculty of Economic and Muamalat, Dr. Asmaddy Haris (USIM) for his kind approval and recommendation, this study could be pursued under full sponsorship. A highly appreciation also addressed to all fellow friends who continuously support and motivate the researcher to everlasting effort in completion this study, those are Prof. Dr. Abdul Rahim Abdul Rahman, Dr. Hydzulkifli Hashim (UUM), Dr. Fuadah Johari (USIM), Dr. Muhammad Ridhwan B. Abd. Aziz (USIM), Mr. Mohammad Noorizzuddin Bin Nooh (USIM), Ustaz Abdullah Jalil (USIM) and also all faculty members in USIM and in the Academy of Islamic Studies University of Malaya. A grateful also dedicated to the Ministry of High Education, Malaysia which sponsored this study.

Further, a special gratitude addressed to all parties involved in the successful of this study especially to the Deputy Director of Islamic Banking and Takaful Department of the Central Bank of Malaysia, Dr. Zainul Hasfi, Mr. Haji Rustam Bin Idris, Deputy Director of Islamic Banking and Takaful Department of Central Bank of Malaysia, Mr. Makhzani Mustapha Ng., Manager, Prudential and Takaful Section of Islamic Banking and Takaful Department Central Bank of Malaysia, Dr. Ronald Rulindo of Islamic Financial Services Board (IFSB) and all fellow members in the Department of Islamic Banking and Takaful, the Central Bank of Malaysia.

A very thankful addressed to all respondents involved in interview sessions especially to Dato' Dr. Mohd Daud Bakar, Professor Dr. Akram Laldin from ISRA, Associate Professor Dr. Ahcene Lahsasna from Inceif and Dr. Amat Taap Manshor from Finance Accreditation Agency (FAA).

The researcher would like to take this opportunity to express a highly appreciation and gratitude to all family members especially to Hajah Adamiah Binti Adam as a mother, which continuously giving support and motivation to complete this study. Special gratitude addressed to the beloved wife Rohani Binti Awang @ Yaacob for her motivation and support.

All these individuals contributed a meaningful favour, guidance, consultation and motivation physically and spiritually to keep the researcher strong in facing challenges in completion this study.

Lastly, the researcher would like to seek forgiveness for the imperfections of this study.

Jazakumullahu khayr al-jaza',

Wassalam.

Mohd Nazri Bin Mohd Noor,

Faculty of Economic and Muamalat,

Islamic Science University of Malaysia (USIM),

Bandar Baru Nilai,

71800, Nilai, Negeri Sembilan.

nazrimn@usim.edu.my

nazri_um@yahoo.com

TABLE OF CONTENT

CHAPTER 3: The Global Hub Process: Malaysia's Vision Towards Becoming the Islamic Finance Global Hub Country

CHAPTER 4: INTIATIVES OF BANK NEGARA MALAYSIA IN POSITIONING MALAYSIA AS A GLOBAL HUB FOR ISLAMIC FINANCE

LIST OF TABLE

PAGE

LIST OF CHART

LIST OF DIAGRAM

PAGE

ATTACHMENT

SUPPLEMENTARY

LIST OF ABBREVIATION

AAOIFI	:	Accounting and Auditing Organization for Islamic Financial Institutions
AB.	:	Abdul
BAFIA	:	Banking and Financial Institution Act
BBA	:	Bay’ Bithaman Ājil
BIMB	:	Bank Islam Malaysia Berhad
BNM	:	Bank Negara Malaysia
CBA	:	Central Bank Act
DFIA	:	Development Financial Institution Act
Ed.	:	Editor
E & Y	:	Ernst and Young
FAST	:	Fully Automated System for Tendering
FSMP	:	Financial Sector Masterplan
GCIBFI	:	General Council for Islamic Banking and Finance Institutions
GCR	:	Global Competitiveness Report
GDP	:	Gross Domestic Products
GFCI	:	Global Financial Center Index
IBA	:	Islamic Banking Act
Ibid	:	*Ibidem* (pada tempat yang sama)
IBFIM	:	Islamic Banking and Finance Institute Malaysia
IFI	:	Islamic Financial Institution
IFSA	:	Islamic Financial Services Act
IFSB	:	Islamic Financial and Services Board
IIFM	:	International Islamic Financial Market
IIRA	:	Islamic International Rating Agency
ILMC	:	Islamic Liquidity Management Centre
IIUM	:	International Islamic University of Malaysia
IOSCO	:	International Organization of Securities Commissions
IRTI	:	Islamic Research and Training Institute
ISRA	:	International Shariah Research Academy for Islamic Finance
Jil.	:	Jilid
Juz.	:	Juzuk
MIFC	:	Malaysia International Islamic Financial Centre
OECD	:	Organization of Economic Cooperation and Development
RENTAS	:	Real Time Electronic Transfer of Funds System
SC	:	Securities Commission
SIDC	:	Securities Industry Development Corporation
SSB	:	Sharī’ah Supervisory Board
SM	:	Sharī’ah Committee
WEF	:	The World Economic Forum

TRANSLITERATION INDICATORS

The indicators are as follows:[1]

i. Consonant Capitals

Arabic Capitals	Name	Latin Capitals
ا	*alif*	a / ’
ب	*ba’*	b
ت	*ta’*	t
ث	tha’	th
ج	*jim*	j
ح	*ha’*	*h*
خ	*kha’*	kh
د	*dal*	d
ذ	*dhal*	dh
ر	*ra’*	r
ز	*zay*	z
س	*sin*	s
ش	*syin*	sy
ص	*sad*	s
ض	*dad*	ḍ
ط	*ta’*	ṭ
ظ	*za’*	ẓ

[1]Jawatankuasa Tetap Bahasa Melayu (1992), *Pedoman Transliterasi Huruf Arab Ke Huruf Rumi*, Kuala Lumpur: Dewan Bahasa Dan Pustaka (DBP).; See also. Akademi Pengajian Islam Universiti Malaya (2001), *Buku Panduan Penulisan Tesis/Disertasi Ijazah Tinggi Akademi Pengajian Islam* Kuala Lumpur: Akademi Pengajian Islam Universiti Malaya, Lembah Pantai.

ع	*'ayn*	'
غ	*ghayn*	gh
ف	*fa'*	f
ق	*qaf*	q
ل	*lam*	l
م	*mim*	m
ن	*nun*	n
و	*waw*	w
ه	ha'	ḥ
ي	*ya'*	y
ة	*ta' marbutah*	h

ii. Vocal Consonant

Vocal	Arabic Capital	Latin Capital
Short	*(fathah)*	a
	(dammah)	u
	(kasrah)	i
Long	آ	ā
	أُوْ	ū
	اِيْ	ī
	اَوْ	aw

Diftong	اَيْ	ay
	يّ	iy/i
	وّ	uww

CHAPTER ONE

1.0 INTRODUCTION

1.1 PREFACE

Malaysia is a country with multi-racial population. It has developed well to become a modern and progressive nation. Among the south East Asia countries, Malaysia appears as the most developed economic country and enjoys peaceful and prosperous melting pot. Malaysian economic in the early stage after its independence on August 31 of 1957 had diversified and expanded without too much reliance on the export of raw materials like rubber and tin, to become a manufacturing-based country with a strong tourism and service industries which contributed to the country's GDP.

Central Banks Act or formerly known as Central Bank Ordinance (CBO) was enacted in 1958. This act has formally allowed the establishment of the Central Bank of Malaysia or known as Bank Negara Malaysia (BNM) on January 26, 1959. The Central Bank of Malaysia (CBM) functions to govern and regulate the banking system in Malaysia and strategize financial plan for the benefit of the country.

The Central Bank of Malaysia as the bank which constitutes the apex of the monetary and banking structure of the country with the objectives to: [2]

- Issue currency and keep the reserves to safeguard the value of the currency;
- Act as a banker and financial adviser to the government;
- Promote monetary stability and a sound financial structure; and
- Influence the credit situation for the advantage of Malaysia.

[2] Bank Negara Malaysia, *The Central Bank and the Financial System in Malaysia*, (Kuala Lumpur: The Central Bank of Malaysia, 1999), 109.

All of the above objectives are interrelated. As the Central Bank of Malaysia is a solely authorized body in Malaysia to issue currency, thus, the prime objective of the Central Bank of Malaysia is to sustain domestic prices in stability condition where it contributes to the economic growth.[3]

In the initial stage of the Central Bank of Malaysia's operation, the central bank plays important roles in developing financial structure to ensure that all economic decisions and plans give impact to the economy as predicted in order to reach the economic targets and objectives. The Central Bank of Malaysia is responsible for planning the necessary framework to ensure a sound financial system in which the banking system functions smoothly and the flow of domestic savings is well managed and channeled to investors. This system will promote the entire development in investment and output.

The initiative to establish the Islamic banking system in Malaysia was made by the Central Bank of Malaysia in the early 1980. As Muslims are required to practice Islam in their whole life including in the financial system, thus, this initiative substantially enables the compliance to the Islamic religion and requirements in the aspect of banking, insurance and financial system. In the Central Bank of Malaysia, a new section to handle the matter pertaining to the Islamic banking system and *Takaful* was established and named as the Islamic Banking and *Takaful* Department of the Central Bank of Malaysia. This section plays a vital role in observing the Islamic banking system in Malaysia as well as strategizing a development plan and prudent policies for the benefit of the Islamic banking and *Takaful* system in Malaysia.

The reason why Islam restricts the application of the conventional system is because of the existence of *Riba* or usury in the conventional financial system. *Riba* in loan puts the borrower in a financial burden situation when the borrower has to pay an

---

[3] *Ibid*., 121.

additional amount besides the actual amount of money loaned out to him. Thus, *Riba* makes the poor becomes poorer and the rich becomes richer; a condition that is unjust and will subsequently affect the social life, which leads to the collapse of the society. Hence, the obligation to avoid *Riba* is among the responsibilities of the Muslims and the Muslim government. In order to fulfill such a responsibility, the government has to work for the establishment of an Islamic banking and financial system. The prohibition of *Riba* is evidenced from al-Quran as Allah says:

.... وَأَحَلَّ ٱللَّهُ ٱلۡبَيۡعَ وَحَرَّمَ ٱلرِّبَوٰاْۚ ....

Meaning: "…. Whereas Allah has permitted trading and forbidden usury...."[4]

(al-Baqarah: 275)

And the word of Allah Taa'la in Surah ar-Ruum:

وَمَآ ءَاتَيۡتُم مِّن رِّبٗا لِّيَرۡبُوَاْ فِيٓ أَمۡوَٰلِ ٱلنَّاسِ فَلَا يَرۡبُواْ عِندَ ٱللَّهِۖ

"And (know that) what you give in usury, so that it may increase in people's property will not increase with Allah (does not bring any good)."[5]

(ar-Ruum: 39)

Considering the consequences of *riba*-based financial system on the economy and society, thus, the best replacement for this system is through the establishment of an Islamic banking and financial system. Amazingly, the Islamic banking system has successfully appeared as an alternative financial system in a short time period, which took only 25 years of the establishment since 1975. In contrast, the conventional

[4] Department of Islamic Development Malaysia, *Tafsir ar-Rahman Interpretation of the Meaning of the Quran*, (Putrajaya, Malaysia: Department of Islamic Development Malaysia, 2007), 82.
[5] *Ibid*., 774.

counterpart took 200 years to appear as a complete banking and financial system in the world.[6]

Many parties are involved in the success of the Islamic banking and finance system. However, the main players who initiated the effort for this success were the Muslim scholars. Muslim scholars motivated people to avoid *riba* in financial transactions and they provided a *Sharī'ah* -compliant recommendation in the form of an alternative Islamic financial contract. Muslim scholars also consulted the governments in forming the Islamic banking system and institutions.

The emergence of the Islamic financial system has brought about a new paradigm to the conventional practitioners to study the advantage of this system. By implementing the prohibited element like *riba, gharār* and uncertainty in the system, the Islamic banking and financial system are of low risk and able to sustain to financial shocks.

This is evidenced through the sustainability of this system in facing the global financial shock, which occurred between the years 2007-2009. During that financial turmoil, many conventional banking institutions were shut down due to the house mortgage crises. However, the Islamic banking systems were not affected by this crisis because the Islamic banking system prohibits the sale and purchase of document of debts. Thus, the Islamic banking and financial system remain stable, productive, resilient, feasible and viable in facing the economic crises.[7]

The Islamic banking and finance in Malaysia has existed for 31 years starting from the commencement of the Islamic Bank in 1983, which was regulated under the Islamic banking Act 1983 until the year 2014. In the latest period, the Islamic Finance

---

[6] Zeti Akhtar Aziz, *Islamic Banking and Finance: Progress and Prospects Collected Speeches: 2000-2006*, (Kuala Lumpur: The Central Bank of Malaysia, 2006), 4.

[7] International *Sharī'ah* Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations*, (Kuala Lumpur: International *Sharī'ah* Research Academy for Islamic Finance, 2011), 3.

industry enters into a liberalization era, which sees the establishment of more Islamic financial institutions in the country.[8]

As Malaysia is in the vision to develop the country as an Islamic finance global hub, hence, some of the matters pertaining to the Islamic financial system have to be reviewed in order to equip the system with the updated version of products, technologies, efficiencies and accuracies. As such, Malaysia is able to keep pace with the global standard of services. Thus, the design of the future Islamic finance plan in Malaysia must be based on this backdrop and criteria of integrated economic development and financial markets.[9]

The Central Bank of Malaysia as the sole regulator of the financial system in Malaysia views the futuristic development of Islamic finance and thus, set up a ten-year plan to guide the pathway of Islamic finance in the specific plan named as the Financial Sector Master Plan (FSMP) to ensure the continued effectiveness, competitiveness and resilience of Islamic finance system.

FSMP is designed with the objective to develop Malaysia as the International Islamic Financial Centre.[10] This plan plays a vital role in upgrading the Islamic finance system in Malaysia to be in tandem with the international standard by adopting the international best practice and standards into the domestic financial system.

Based on this target and objective, FSMP underlined 115 points of recommendations to enhance the Islamic finance system in Malaysia which catered many fields of financial system including the insurance sector, banking sector, Islamic banking and *Takaful*, alternative modes of financing, development and financial institutions and Labuan Offshore Financial Centre.[11]

---

[8] Bank Negara Malaysia, "Overview of Islamic Finance in Malaysia," retrieved on 27 December 2011, http://www.the Central Bank of Malaysia.gov.my/microsites/financial/0204_ib_*Takaful*.htm.
[9] Bank Negara Malaysia, *Financial Sector Master Plan*, (Kuala Lumpur: The Central Bank of Malaysia, 2001), 15.
[10] *Ibid*., 28.
[11] *Ibid.*, 121-124

FSMP has successfully evolved Islamic finance in Malaysia and made a significant development towards Malaysia's Islamic finance performance. According to a Bloomberg report on 7th October 2011, Malaysia's Islamic banking assets rose 15 percent to 389.3 billion ringgit ($123 billion) in the first seven months of 2011, strengthening the country's position as the global hub for *Sharī'ah*-compliant financing.[12] Simultaneously, Malaysia was recorded as the biggest *Sukuk* issuer, which represents 62.7% of total global *Sukuk* as reported in 2011, which positioned Malaysia as a leader in *Sukuk* issuance. Bursa Malaysia was reported as a destination where *Sukuk* were listed the most and becoming as the top *Sukuk* destination in comparison to other places. As at the end of July 2011, about 19 *Sukuk* were issued amounting to RM88.3 billion. This improvement indicates that Malaysia currently appears as an attractive place for global Islamic investment destination.

As an overview for the existence of Islamic finance around the world, the Islamic finance system is now offered in over 75 countries. There are more than 600 Islamic finance institutions established in Muslims and non-Muslims countries. Obviously, the number of Islamic finance institutions recorded a significant growth and constantly received a good acceptance among peoples around the world. This growth has made Islamic finance parallel to the conventional financial institutions. Previously, a new financial area existed as a result of regulatory changes in non-ordinary places but now it emerges among the significant area in the international financial system.

As in 2011, the Bankers reported in their top 500 Islamic Financial Institutions report that there are significant growths of Islamic finance industry, which charted up to 21% with assets reaching USD 1 trillion.[13] Globalization era in the financial sector has brought Malaysia into a new sphere of domestic and international financial background.

[12] Bloomberg Businessweek, "Malaysian Islamic Banking Assets Rise 15 percent to $123 Billion," retrieved on 27 December 2011, http://www.businessweek.com/news/ 2011-10-07/malaysian-Islamic-banking-assets-rise-15-percent-to-123-billion.html.

[13] Zeti Akhtar Aziz, "The New Islamic Finance Landscape," (Keynote Address by the Governor of The Central Bank of Malaysia, presented on 15th November 2011 at Sasana Kijang, Kuala Lumpur).

These development is steered by the advance of technology comprises the information and communication technology which eliminated barriers among countries around the world.[14]

The globalization agenda has an impact on the conventional financial industry. Hence, several studies have been conducted to address the related problems in order to propose solutions to fix the loopholes. However, the impact of globalization on Islamic banking and finance is still in its observation stage and hence, it is premature to conclude any positive or negative impact on the system.

The initiative to develop Malaysia as an Islamic finance global hub has attracted studies on the positive and negative impact of this policy. The internationalization of domestic industries is no doubt has enhanced Islamic finance services. However, the global hub policy opens the domestic industry to international participation and hence, will create a rigorous competition between local and foreign Islamic finance institutions. Should there be any effect on local Islamic financial institutions by this competition, the government has to prepare a contingency plan to secure the affected parties. Therefore, this study attempted to find out the possible negative impacts that may arise during the implementation of this policy.

In addition, this study also attempted to develop a framework to evaluate Islamic finance global hub since many countries claim themselves as Islamic finance global hubs. This framework is important to be developed in order to determine the distinct characteristics of an Islamic finance global hub.

[14] *Ibid.*, 37.

1.2 RESEARCH BACKGROUND

The Central Bank of Malaysia functions as a sole regulator of banking and financial system in Malaysia and is responsible to design a future pathway for the excellence of the Malaysian banking and financial system. One of the prime initiatives taken by the CBM is a setting up of a ten-year Financial Sector Master Plan (FSMP). This plan has several recommendations, which aim to create a robust structure of banking and financial system that consists of empowering corporate governance of banks and encourages close cooperation among banking institutions. This strategic plan and several recommendations as well as proposals are structured with the prime and paramount objectives to position Malaysia as an Islamic finance global hub.

Obviously, the Central Bank of Malaysia has made continuous effort to facilitate the country as an Islamic finance global hub. However, there are challenges that stand ahead together with obstacles that the CBM has to face in order to realize this vision. There are also effects from the decision to liberalize the domestic Islamic finance market to foreign Islamic finance institutions that attracts competition between both Islamic finance institutions.

To identify the challenges, obstacles and effects from the global hub policy may request a study on this topic together with a proposal to define the accurate way to measure the Islamic finance global hub country. The specific measurement of an Islamic finance global hub is important since many countries around the world claim themselves as Islamic finance global hubs. Famous Islamic finance countries like Malaysia, UAE, London and Qatar are competing against each other to market their countries or cities as Islamic finance global hubs. The emergence of new Islamic finance countries such Singapore, Hong Kong and others, they are designing strategic plans to become as a conducive place for Islamic finance inclusively by providing a supportive regulatory system, giving more tax incentives and many more measures to make the country as an attractive Islamic finance market in the world.

Based on this backdrop, this study was conducted to determine the challenges encountered by CBM in their way to position Malaysia as a global hub for Islamic finance as well as to study the positive and negative impacts from certain policy pertaining to this vision. Furthermore, this study attempts to develop a framework based on Islamic value in order to assess the Islamic finance global hub countries.

1.3 PROBLEM STATEMENT

Since the introduction of the Islamic financial system in Malaysia in 1983, the country has progressed markedly despite an increasingly liberalized and competitive environment. Malaysia's Islamic financial system, based on the concept of profit-sharing as opposed to the use of interest in the conventional financial system, has evolved as a competitive component of the overall financial system. It complements and competes with the conventional financial system and is recognized as a driver of economic growth and development. The Central Bank of Malaysia had intensified efforts to position Malaysia as an Islamic finance global hub. Based on this background, the problem statement of this thesis could be summarized on the following matters:-

1. What is the Malaysia's Islamic Finance Framework?
2. What is the meaning of global hub and how the process expands?
3. What are the initiatives taken by the Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic finance and market?
4. What are the possible challenges faced by the Central Bank of Malaysia in developing Malaysia as a global hub for Islamic finance?
5. What is the best method to evaluate an Islamic finance global hub country?

All of these questions helped to develop a structure of this study, which led to further development of ideas and scholarly views. The first question is on Malaysia's Islamic finance framework which aims to understand the background of the system and how the system functions. The second question is to explore the literal and historical meaning of global hub and how does it evolvement. The third question is on the initiatives taken by the Central Bank of Malaysia to develop Malaysia as an Islamic finance global hub. The fourth question is to unravel the challenges that may be faced by the Central Bank of Malaysia. The fifth question is on the assessment framework to evaluate an Islamic finance global hub country.

1.4 RESEARCH OBJECTIVE

The main objectives of the study are:

1. To study Malaysia's Islamic finance framework.
2. To explore the process of Islamic finance global hub evolution.
3. To study the initiatives taken by the Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic banking and finance.
4. To examine the challenges that must be addressed by the Central Bank of Malaysia in the effort to position Malaysia as a global hub for Islamic banking and finance.
5. To study comparatively assessment bodies in evaluating global hub countries and to propose a new framework in measuring Islamic Finance Global Hub countries.

1.5 SIGNIFICANCE OF STUDY

This study particularly provides a critical analysis on the idea of positioning Malaysia as a global hub for Islamic finance. Hence, the study has an important contribution in the following areas:

1. This study will benefit the Central Bank of Malaysia in determining the positive and negative impacts of the Islamic finance global hub policy.
2. This study will provide better enlightenment of Islamic finance global hub among the Islamic finance players which constitute of Islamic banking institutions, *Takaful* operators and Islamic capital market.
3. This study is an additional reference in the Islamic finance where it will benefit future research regarding the global hub study in Islamic finance.
4. This study is important for the authorities to raise concern on the effects of Islamic financial liberalization and to make an appropriate preparation to manage any possible risks accordingly.

1.6 RESEARCH SCOPE

The scope of this study is as follows:

1. This study will focus on the initiatives of the Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic finance.
2. Islamic finance system in this study refers to Islamic banking, Islamic insurance (*Takaful*) and Islamic capital market.
3. This study attempted to examine issues and challenges that may possibly appear in the course of developing Malaysia as an Islamic finance global hub country. It also attempted to propose suitable recommendations to manage the challenges.

4. This study attempts to identify the potential of Malaysia towards becoming a global hub for Islamic finance which includes its political stability, future Islamic finance products, international confidence and others.
5. Given that this study had been conducted in 2010. Hence, the acts and regulations discussed in this study are in the Islamic Banking Act 1983 and the Banking and Financial Institution Act 1989 before the replacement of these acts in 2013 with the Islamic Finance Services Act 2013 or known as (IFSA). However, a brief introduction of IFSA is also included in this study.

1.7 DEFINITION OF TITLE

The title of this thesis is: "The Roles of the Central Bank of Malaysia in Positioning Malaysia as a Global Hub for Islamic Finance". This study reviewed plans and strategies taken by the Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic finance. This study is important in order to gauge the readiness of Islamic finance in Malaysia in providing the international standard of Islamic finance services towards local and global customers worldwide. The Islamic finance sectors involved in this vision consist of the Islamic banking sector, the Islamic insurance (*Takaful*) and the Islamic Capital market. In addition, this study focuses on the sustainability of each Islamic finance sectors and its performance along the period of the establishment in Malaysia.

1.8 RESEARCH METHODOLOGY

1.8.1 METHOD OF DATA COLLECTION

Data collection involves the efforts of collecting, interpreting the data and recording the information obtained. Before data to be collected, any necessary measuring instruments must be identified and perhaps developed. This applies a mixed method namely qualitative and quantitative which used to conduct interview and survey questionnaire methods. However, method of interview as a qualitative method becomes as a main method and subsequently supported by the survey method. The following table summarizes data collection process in both methods:

Table 1.1: Phases in the data Collection Process for Qualitative and Quantitative Research.[15]

Qualitative Data Collection	**Phases in the Process of Research**	**Quantitative Data Collection**
- Purposeful sampling strategies - Small number of participants and sites	Sampling procedures	- Random Sampling - Adequate size to reduce sampling error and provide sufficient power
- From individuals providing access to sites. - Institutional review boards - Individuals	Permissions Needed	- From individuals providing access to sites. - Institutional review boards. - Individuals
- Open-ended interviews - Open-ended observations - Documents - Audiovisual materials	Information to be collected	- Instruments - Checklists - Public Documents
- Interview Protocols - Observational Protocols	Recording the Data	- Instruments with scores that are reliable and valid
- Attending to field issues - Attending to ethical issues	Administering data collection	- Standardization of procedures - Attending to ethical issues.

Sources: J.W. Creswell & V.L. Plano Clark, 2007.

15 J.W. Creswell and V.L. Plano Clark, *Designing and Conducting Mixed Methods Research*, (California: Sage Publications, 2007), 7.

According to J.W. Creswell and V.L. Plano Clark mixed method is defined as:[16]

Mixed method research is a research design with philosophical assumptions as well as methods of inquiry. As a methodology, it involves philosophical assumptions that guide the direction of the collection and analysis of data and the mixture of qualitative and quantitative approaches in many phases in the research process. As a method, it focuses on collecting, analyzing and mixing both quantitative and qualitative data in a single study or series of studies. Its central premise is that the use of quantitative and qualitative approaches in combination provides a better understanding of research problems than either approach alone.

A qualitative method was utilized to determine the function of the Central Bank of Malaysia in positioning Malaysia as an Islamic finance global hub country. Through this method, this study attempts to understand the transformation of a country to become an Islamic finance global hub country from its starting point as a national Islamic finance country. Several data from annual report, Bank Negara Malaysia Financial Sector Master Plan, books, journals and other library research sources were analyzed to develop a robust understanding of this study. An interview method was also applied to seek views from the prominent Islamic finance scholars to get clearer views pertaining to the challenges and several potential opportunities for Malaysia in becoming as an Islamic finance global hub country.

A quantitative method was employed by using a survey method to determine the reliability of the Islamic finance global hub framework. This framework is a proposal framework to measure the Islamic finance global hub countries.

[16] *Ibid.*,5.

1.8.2 Main Method: Interview

Interview is defined as a conversation with a purpose.[17] It is an interactional communication process, which involves the asking of questions by the interviewer for the specific purpose of obtaining research-relevant information and answering of questions by the interviewee.[18] The possible number of respondent is determined based on Cresswell[19] methodology, which views that the acceptable number of interviewees is between 1 to 2 persons and up to 30 to 40 people.

Mohamad Najib[20] and Nixon[21] view, interview as one of the several methods to provide additional important data in depth and detail information regarding a certain issue, which is not available to be acquired via surveys and other methods. In the other hand, Cresswell[22] states that interview method could provide useful information after a researcher fails to observe the respondents directly.

According to Limputtong and Ezzy[23], among the advantages of using interview are:

1. It enables the exploration of the subjective meanings and interpretations of someone's experience;
2. It allows social aspects of life such as social processes and interactions to be studied via negotiation, which aspects cannot be studied through other methods;
3. It allows the understanding and new theories to be constructed during the research process;

[17] Kahn R.L. & Cannell, C.F., *The Dynamics of Interviewing: Theory, Technics and Cases* (New York: Wiley, 1957).
[18] Puvenesvary, M.. Interviews. In Puvenesvary, M., Abdul Rahim, R., Sivabala Naidu, R., Badzis, M., Mat Nayan, N.F. & Abd. Aziz, N.H., *Qualitative Research: Data Collection & Data Analysis Techniques.,* (Sintok: UUM Press, 2008).
[19] Cresswell J.W., *Educational Research – planning, conducting and evaluating quantitative and qualitative research*, Ed.2, (New Jersey: Pearson Merril Prentice Hall, 2005), 375.
[20] Mohamad Najib, *Penyelidikan Pendidikan.* (Skudai: Penerbit Universiti Teknologi Malaysia, 1999), 115.
[21] Nixon, J., *Evaluating the whole curriculum,* (Philadelphia: Open University Press, 1992), 87.
[22] Cresswell J.W., *Educational Research – planning, conducting and evaluating quantitative and qualitative research*, 375.
[23] Liamputtong, P. & Ezzy, D., *Qualitative Research Methods,* (Victoria: Oxford University Press, 2005).

4. The responses from the respondents are not influenced by the presence of friends for individual interviews or in-depth interviews; and
5. Respondents generally feel appreciative of the interview as it is a chance to share their experience.

There is a lack of consistency on the terms used to refer to the different types of interview, namely the *structured, unstructured* and *semi-structured* interview. Overall, this study uses the semi-structured interview. The semi-structured interview is amidst the extremes of the structured and unstructured interviews. A set of questions is commonly outlined prior to the interview session. The interviewer is free to explore, probe and ask questions that will elucidate and illuminate a particular topic.[24] This method ensures that the interviewer allocates and adjusts wisely the limited time available in an interview situation. The questions are useful, in order to keep the interaction focused, but permits the propositions through individual perspectives and experiences. However, the flexibility given may result in different interviewers asking somewhat different questions of different interviewees, thus, reducing the comparability of the responses obtained.[25]

This method of interview was used in order to seek views from Islamic finance regulators and players regarding the CBM's initiatives in positioning Malaysia as a global hub for Islamic banking and finance. The interviews were specifically to seek opinions from CBM's personnel, *Sharī'ah* Advisory Council members, players and scholars in Islamic Banking and Finance institutions, as well as academicians and other related parties. A collective view from the authorized participants provides reliable thought on Islamic finance global hub. The interview analysis is organized in chapter five and chapter six.

[24] Patton, M.Q., *How to Use Qualitative Methods in Evaluation*, (SAGE Publication, 1987).
[25] Lynch, B.K., "*Language Program Evaluation: Theory and Practice*," (New York: Cambridge University Press, 1996).

1.8.2.1 Interview Validity and Reliability

Interview protocol was developed by the researcher to get respondent's reaction towards the policy of the Central Bank of Malaysia in determining the direction of Islamic financial sector in Malaysia especially in positioning Malaysia as Islamic finance global hub. This method is applied in order to get evidence and confirmation on the policy of the Central Bank of Malaysia and the related issues accordingly.

The interview process begins with the appointment of interview date between the researcher and the respondents. Then, the permission acquired from all respondents to record the discussions using a voice recorder and notes writing. Further, the interview data will be compiled and subsequently will be analyzed accordingly.

1.8.2.2 Respondents

Several series of interviews were conducted specifically to seek opinions from the CBM's personnel, *Sharī'ah* Advisory Council members, players in Islamic Banking and Finance institutions, scholars in Islamic banking and finance, academicians and other related parties. A collective view from the authorized participants will provide a reliable thought regarding to the research.

1.8.3 Supportive Method: Survey Method

A survey method was used to gather respondent's views regarding to the Islamic Finance Global Hub Index. This index consists of various variables which are aiming to measure the Islamic finance countries and categorizing the country into certain level which labeled as National, Regional, International and Global hub. This method of study will be managed under chapter six which studies the new Islamic finance global hub index as a proposal framework to measure Islamic finance countries. Most scales currently uses in survey research appear to be based on the summation model originally set forth by Liker (1932).[26]

The survey distributed consists of several parts:

i) Islamic Finance Index: The Subjects and the Description of the Index

ii) Demographic Information

iii) Appendix (Islamic finance Global Hub Framework)

1.8.3.1 Unit of Analysis

According to Earl Babbie,[27] formal social organizations may also be the units of analysis in social scientific research. For example, a researcher might study corporations, by which he or she implies a population of all corporations. Individual corporations might be characterized in terms of number of employees, net annual profits, gross assets, number of defense contracts, percentage of employees from racial or ethnic minority groups, and so forth.

In accordance to this study, the target respondents comprise the following groups:

1. Regulator
2. Banker
3. Researcher

"Regulator" is referred to the top management in the Department of Islamic Banking and Takaful of the Central Bank of Malaysia. The total number of staffs serve with the department in the year assessment in 2014-2015 are 92 persons. There are five divisions in this department namely Strategic Development and Market Surveillance, Internationalization Strategy and Development, Talent Development and Strategic Communication, Prudential Policy Development and *Sharī'ah* department. The sample

[26] John A.Sonquist and William C. Dunkelberg, *Survey and Opinion Research: Procedures for Processing and Analysis*, (Eaglewood Cliffs, New Jersey: Prentice Hall, 1977), 262.

[27] Earl Babbie, *The Practice of Social Research, 9th Edition*, (United States of America: Wadsworth, 2001), 96.

from this group was determined by selecting the head of the division and two managers in each division. Therefore, the total number of sample to represent this group of regulator is 15. However, only 14 set of questionnaires were returned. The selection of the Islamic finance and *Takaful* department staffs of the Central Bank of Malaysia is due to their function as a task group in handling and supervising matters pertaining to Islamic banking and finance in Malaysia. Their involvement in designing regulations, plans and strategies in the beginning of the establishment of Islamic bank in Malaysia have made themselves as most suitable samples to assess matters regarding to the Islamic banking and finance including the Islamic finance global hub index.

"Banker" is referred to officer work in local Islamic banks in Malaysia. Based on 2015 data as stated in CBM record, there are 10 local Islamic banks operate in Malaysia and one corporation bank. In this study, the samples are involve three local Islamic banks namely Bank Islam, Maybank Islamic and Hong Leong Islamic Bank to represent local Islamic banks and one corporative bank namely Bank Rakyat. The distribution of survey questionnaires must be approved by the management of each bank and hence, there are different numbers of questionnaires distributed in the said banks.

The reason of the selection of Bank Islam as a sample is due to its historical background as the first Islamic bank established in Malaysia. 20 sets of questionnaires were distributed randomly to the officers in the bank in various departments. The number of returned questionnaires is 16. Maybank Islamic bank was selected as a sample due to its size as the largest bank in Malaysia. 10 sets of questionnaires were distributed to the bank's senior officers and the returned sets of questionnaires were 5 sets. Hong Leong Islamic bank was selected to represent the private owned bank. Ten set of questionnaires were distributed to the respondents and only six set of questionnaires were returned back. Bank Rakyat was selected as a sample to represent the corporative bank. 10 set of questionnaires were distributed and the returned set of questionnaires was 8 sets. All banks gave consents to answer 10 questions whilst Bank Islam permits 20 questionnaires. However, the number of returned questionnaires is less than the distributed questionnaires. The following data shows the number of returned questionnaires:

1. Bank Islam: 16
2. Maybank Islamic: 5
3. Hong Leong Islamic: 6
4. Bank Rakyat: 8

Overall, collecting data among the bankers experienced a though effort and patience due to their time constraint in answering the questionnaires. In addition, permission from the management is the first condition to be approved prior the distribution of the questionnaires being executed.

The third group is researchers where it refers to the number of researchers involve in Islamic banking and finance research. The level of researcher involve in this survey are lecturers, senior lecturers and Professors. This group of researcher are having specialty in Islamic banking and finance where some of them are *Sharīʼah* advisor to local Islamic banks, the economist and consultant in many institutions. All researchers were from two universities namely the International Islamic Science University (USIM) and University Putra Malaysia (UPM). This sample of researcher is considered as a supportive sample to the two previous groups (regulator and banker).

The following table is the list of samples in this study:

Table 1.2: Sample of Survey

Sample	**Type**	**Returned Questionnaires**	**Responding Percentage**
Regulator	BNM	14	93 %
Bankers	Bank Muamalat	8	80 %
	Hong Leong	6	60 %
	Maybank	5	50 %
	Bank Islam	16	80 %
Researcher	UPM USIM	6 12	100 % 100 %
	Total	67	

Therefore, the total samples involve in this survey are 67 samples. This number represents the above three groups in evaluating the framework of Islamic finance global hub index.

1.8.3.2 Survey Design

This survey consists of 30 items. All items were measured by five items based on a five-point scale ranging from 1 to 5 (1: Strongly Disagree; 2: Disagree; 3: Neutral; 4: Agree; 5: Strongly Agree). Section II provides demographic data on each respondent. A diagram of Islamic Finance Global Hub index will be enclosed in the form to provide clearer image on the index.

1.8.3.3 Validity and Reliability of Measures

1.8.3.3.1 Validity

In order to measure the validity, this study applies Expert Review method. An expert panel usually comprises independent specialists. The panel specialists arrive at conclusions and recommendations through consensus. The expert is specifically appointed for the evaluation, and in conformity with standard procedures. The experts give comments and recommendations on the precise conclusions regarding to the questionnaire. Overall, the using of expert review method benefits the research by enhancing the following matters:

1. Studying very specific fields requiring a high level of competence.
2. Studying subjects for which other tools are difficult to implement at a reasonable cost.
3. Carrying out limited-scope evaluations.
4. Assisting the evaluators in their conclusions on a subject in complex evaluations.
5. Providing assistance in the drafting of final conclusions relating to the possible impacts of a programme in ex-ante evaluations.

To validate the variable of index, the researcher approaches three professional individuals who are having expertise in the field namely Prof. Dr. Abdul Rahim Abdul Rahman,[28] Prof. Dr. Zainal Abidin Bin Mohamed[29] and Dr. Nuradli Ridzwan Shah Bin Mohd Dali.[30] Three sets of surveys of index were provided to all experts to review and to propose available comments in order to enhancing the survey. As a result, the amendment has been made based on their comments and proposals. The objective of the survey is to seek respondents view on the Islamic finance global hub index which consists of variables and definitions of each variable.

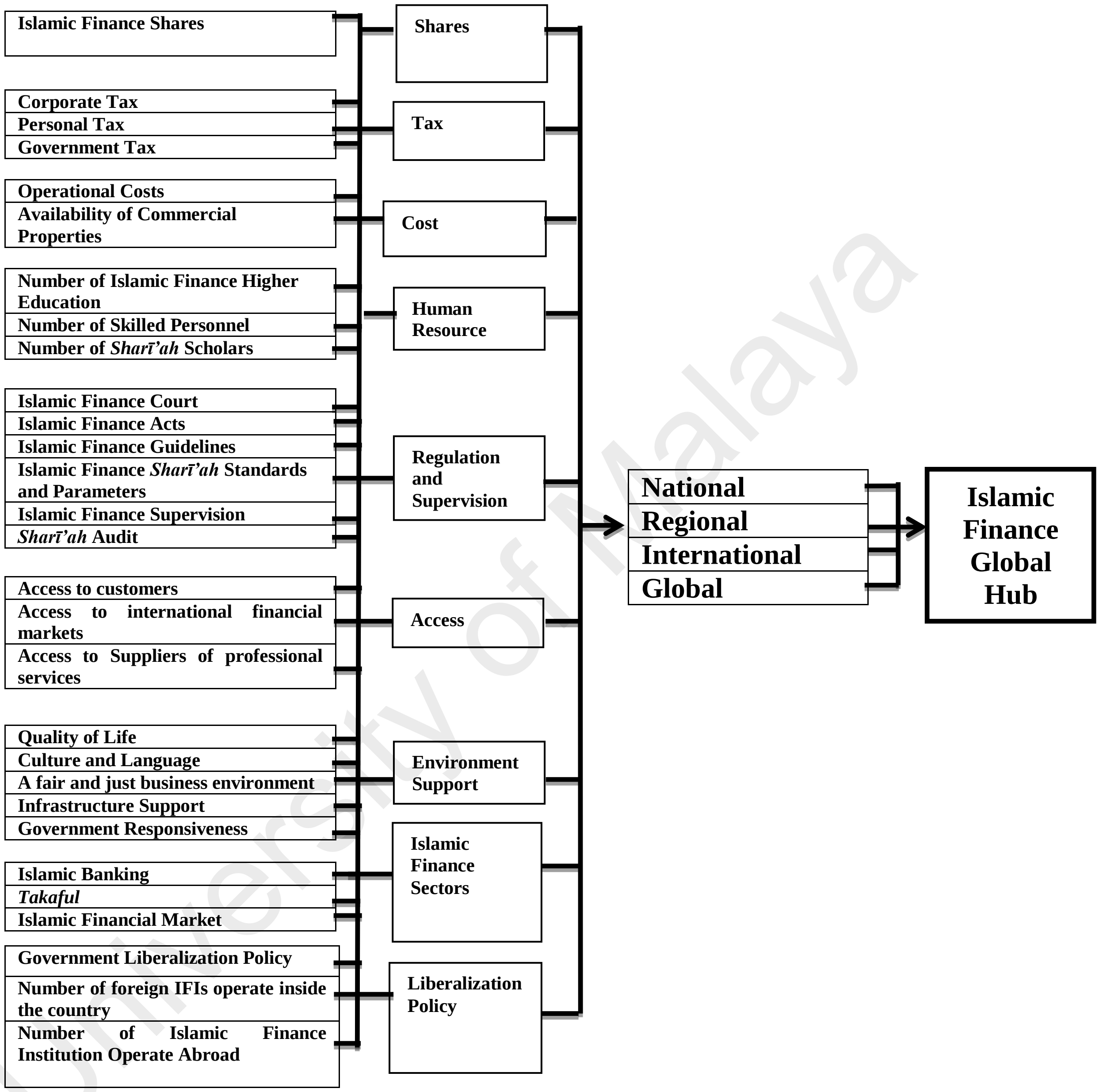
[28] Prof. Dr. Abdul Rahim Abdul Rahman is currently a Professor and attached with the Faculty of Economics and Muamalat, the Islamic Science University of Malaysia (USIM) based in Nilai, Malaysia. Beside full-time at USIM, he is also attached with the International *Sharī'ah* Research Academy in Islamic Finance (ISRA) based in Petaling Jaya, Malaysia, as a Research Fellow.

[29] Prof. Dr. Zainal Abidin Bin Mohamed, is currently a Professor and works with Faculty of Economics and Muamalat, the Islamic Science University of Malaysia (USIM) based in Nilai, Malaysia. His current position is as the Deputy Dean of Graduate School of Muamalat in the Faculty of Muamalat, USIM.

[30] Dr. Nuradli Ridzwan Shah Bin Mohd Dali, is a senior lecturer at the Faculty of Muamalat, Islamic Science University of Malaysia.

The following diagram is a proposal framework for Islamic finance global hub index as displayed to the experts:

Diagram 1.1: Islamic Finance Global Hub Framework:



Each item in the index has its own descriptions. The following table detailed all the descriptions embedded in each item:

Table 1.3: Description of item of Islamic finance global hub index

Item	Description
Shares and Quantities	
Islamic Finance Shares	To identify Islamic finance Shares in the country which will indicate the strength of Islamic finance institutions in term of demand, size and performance.
Number of foreign Islamic finance Institution Operate in the country	To observe the policy of the government in term of liberalization policy to position the country as the world Islamic finance service provider.
Number of Islamic Finance Institution Operate Abroad	To identify the performance of local Islamic finance institutions in order to determine the efficiency, sustainability, competency and international standard services.
TAX	
Corporate Tax, Personal Tax, Government Tax and Other Related Taxes	Transparency, clarity, simplicity and predictability are vital to be observed regarding to the tax matter.
Environment Support	
Quality of Life	Standard and quality of living promote pleasant working environment and peace of mind.
Culture and Language	Multi lingual and good cultures of populations are among important factor of country's internationalization policy.
A fair and just business environment	A fair and just business environment will ensure sound competition, fair legal decision and give the right to the entitled parties.
Infrastructure Support	To determine the availability of infrastructure support such as ICT speed and security, electricity and water supply, highway networks and connections and other related infrastructure.
Government Responsiveness	The government plays important role in developing sound domestic business through the affective regulation, tax reduction and fast responsive towards claims and corrections.
Cost	
Operational Costs	The operational cost is important to be included in the assessment as this will determine the capability of the Islamic financial institutions to operate within the appropriate cost.
Availability of Commercial Properties	The availability of commercial properties in the city country will promote the presence of foreign Islamic financial institutions to open the business inside the country.
Human Resources	
Number of Islamic Finance Higher Education	The existence of number of higher education/ learning will promote the produce of many human capital sources and hence will provide the institutions variety of options

	in choosing the most suitable staff.
Number of *Sharī'ah* Scholars	*Sharī'ah* scholars play a very important role in Islamic finance as they are function to approve Islamic finance products and policies, to provide *Sharī'ah* opinions and to clarify any ambiguities in Islamic finance.
Regulation and Supervision	
Islamic Finance Court	The establishment of Islamic finance court is important in Islamic finance system to resolve the Islamic finance disputes.
Islamic Finance Acts	The sound, affective and robust acts' framework will ensure the efficiency of the Islamic financial system.
Islamic Finance Guidelines	The issuance of Islamic finance guidelines will ease the function of the system.
***Sharī'ah* Standards in Islamic Finance**	*Sharī'ah* standard in Islamic finance is important to streamline various *Sharī'ah* interpretations and rulings in Islamic finance.
Islamic Finance Supervision and Audit	Islamic finance system is also exposed to the abuse action and wrongdoing from any person who will put the system incompliance with *Sharī'ah*. Thus, the supervision will ensure any mistakes are fixed and replaced into the right order.
Access	
Access to Customers	Access to customers means physical proximity to clients.
Access to International Financial Markets	Refers to the IFI's networking with international players to facilitate cross border transaction.
Access to Suppliers of Professional Services	To observe the availability of professional services such as IT specialist, expert accountants, legal firms and others.

Table 1.4: Description of the National. Regional, International and Global Hub of Islamic financial country

National Islamic Financial Country	A country which conduct Islamic financial services within National level. The Islamic financial institutions operate inside the country and there are no license approved to the foreign Islamic financial institutions to operate inside the country.
Regional Islamic financial Country	Is defined as a country that provides Islamic financial services within the regional areas. Islamic financial institutions operate businesses within the region and there are also licenses opened to the regional Islamic financial institutions.
International Islamic financial Country	Refers to a country where the Islamic financial institutions operate in the international level. The country also open licenses for foreign Islamic financial centres to operate inside the country. A large volume of cross-border transactions is conducted, whereby these transactions include at least two locations in different jurisdictions.
Islamic Finance Global	The most integrated places for Islamic financial services

Hub Country	institutions to connect international, national and regional financial services participants directly.

1.8.3.3.2 Reliability

Reliability of a measure is established by testing for both consistency and stability.[31] This research will adopt consistency, which represents whether all the items are measuring the same underlying construct. The most widely used consistency reliability is the *Cronbach's alpha*.[32] According to Sekaran, *Cronbach's alpha* is a reliability coefficient that indicates how well the items in a set are positively correlated to one another. Generally, agreed upon lower limit for *Cronbach's Alpha* is 0.7.[33] According to George & Mallery,[34] a rule of thumb pertaining to *Cronbach's Alpha* values that have been applied to most situations is shown in Table 1.2:

Table 1.5: Value Range of Cronbach's Alpha

Alpha	Indicator
More than 0.9	Very Good
0.8	Good
0.7	Acceptable
0.6	Questionable
0.5	Weak
Less than 0.5	Unacceptable

Source: George & Mallery, 2001

[31] Sekaran U., *Research Methods for Business: A Skill Building Approach,* (USA: John Wiley & Sons, Inc., 2003).
[32] Bearden, W.O, Netemeyer, R.G., *Handbook of Marketing Scales-Multi Item Measures for Marketing and Consumer Behavior Research,* (Thousand Oaks, California: SAGE Publications, Inc., 1999).
[33] Hair, J.F., Black, W.C., Babin, B.J. & Anderson, R.E., *Multivariate Data Analysis,* (Delhi, India: Pearson Education Inc., 2010).
[34] George, D. & Mallery, P., *SPSS for Windows Step by Step: A Simple Guide and Reference, 10.0 Update,* (3rd ed.)., (Canada: Allyn and Bacon, 2001).

1.8.4 Data Analysis Method

1.8.4.1 Analysis of Interview Data

This analysis begins with the transcription of interviewed data in verbatim way as answered verbally by the respondent. The raw data were transcribed on paper and coded subsequently. Then, the data will be categorized after having a reduction process, based on specific theme. This data analysis is consistent with content analysis proposed by Patton.[35]

1.8.4.2 Analysis of Survey Data

A data analysis method is very important to ensure the quality of research. In this research, the data collected through survey were analyzed by using SPSS software. 100 survey sets were distributed; however the returned survey sets were 67. A total of 67 survey sets were analyzed by entering the data into excel sheets on the SPSS software in numerical form based on the number of responses for each items. Each and every response had its own code. The respondents need to answer all of the items. After all the information of the all items entered into the system, then the researcher started analyzing the information.

1.8.4.3 Mean Analysis

The *mean* is the arithmetic average of the scores and is the most frequently used measure of central tendency. It is calculated by adding up all of the scores and dividing that total by the number of scores. In general, the mean is the preferred measure of central tendency. It is a simple statistical model of the centre of a distribution of score.[36]

[35] Patton, M.Q., *Qualitative Evaluation and Research Method*, 11.
[36] Field, A., *Discovering Statistics Using SPSS.* (3rd ed.)., (London: SAGE Publications Ltd., 2009).

According to Landrum,[37] the arithmetic mean is a fundamental statistical concept and is considered to be a core topic in introductory statistics courses.

The formula used to calculate the mean can be found in the following:[38]

$$\bar{x} = \frac{\Sigma Xs}{n}$$

Where $\bar{x}$ (Read X-bar*) = Sample mean
Σ The Greek letter uppercase sigma = sum, or add up, all the items to the right of this symbol.
Xs= All scores contain in the data set
N= Total number of scores in the data set

*Note: The Greek letter of μ (mu) is used in place of X-bar when computing the mean for a population.

In addition, the mean is typically accompanied by its standard deviation.[39] The standard deviation (SD; also seen in other statistics literature as sd, s, S) is simply the square root of the variance; that is, it's the square root of the average squared deviation from the mean. Basically, it tells us how far the average score in a distribution varies from the mean. By "unsquaring" the variance, the standard deviation represents a conversion back to the unit of measure used with the original scores, making it much more interpretable than the variance. It's this added descriptive value that makes it the most widely used measures of dispersion.[40]

As an index of variability, the more the scores in a distribution are spread out, the larger the standard deviation will be. In turn, when scores are tightly compacted and not widely dispersed, the smaller the standard deviation will be found. In the rare instance where all the scores in a distribution are equal, both the standard deviation and variance will be 0. [41]

[37] Landrum, R.E., "Core Terms in Undergraduate Statistics," *Journal Teaching of Psychology*, (32 (4), 2005), 249-251.
[38] *Ibid.*,91.
[39] *Ibid.*, 92.
[40] *Ibid.*,109.
[41] *Ibid.*

1.8.4.4 Mixing the Data

Analyzing data of the Islamic finance global hub index requires a mix data analysis which comprises survey and interview data analysis. This method was applied in chapter six. By mixing the data set, the researcher provides a better understanding of the problem than if either dataset had been used alone.[42]

1.8.4.4.1 Designing and Conducting Mixed Methods Research

Diagram 1.2: Multiple Studies:

Study 1: Quantitative Study with Reported Results → Study 2: Qualitative Study with reported results → Study 3: Quantitative study with reported results → Etc.

The basic premise of the definition is that the combination of quantitative and qualitative approaches provides a better understanding of research problems than either approach alone.[43]

Among the advantage of using a mixed method research as highlighted by J.W. Creswell and V.L. Plano Clark is detailed as follows:

1. Mixed methods research provides strengths that offset the weaknesses of both quantitative and qualitative research.
2. Mixed method research provides more comprehensive evidence for studying a research problem than either quantitative or qualitative research alone.
3. Mixed methods research helps answer question that cannot be answered by qualitative or quantitative approaches alone.
4. Mixed methods encourages researches to collaborate across the sometimes relationship adversarial relationship between quantitative and qualitative researchers.

[42] J.W. Creswell and V.L. Plano Clark, *Designing and Conducting Mixed Methods Research*, 7.
[43] *Ibid.*, 8.

5. Mixed method research encourages the use of multiple worldviews or paradigms rather than the typical association of certain paradigms for quantitative researchers and others for qualitative researchers.
6. Mixed method research is "practical" in the sense that the researcher is free to use all methods possible to address a research problem.

1.9 LITERATURE REVIEW

The important roles of a central bank, among others are to prudently implement the monetary policy, to ensure sound financial system stability, to play roles in supervision, to act as a banker and adviser to the government, to become a lender of last resort, to formulate economics and monetary policy for the benefit of the country. With regard to the literature review, there are three main headlines related to the topic, which are the Central Bank Supervision, Financial Liberalization and Islamic banking and finance in Malaysia.

The prime objective to review central bank supervision was to examine the function of the central bank in controlling domestic banking and financial system. This literature provides strong evidence on the function of the central bank as a sole regulator in supervising local financial institutions. This literature proves the roles of the central bank in supervising and strategizing plans for the benefit of banking and financial institutions in the country inclusively the plan to design the country system for instance to position the country as Islamic finance global hub.

The financial liberalization issue is vital to be reviewed because the global hub policy liberalizes local Islamic financial institutions and opens local market to foreign Islamic financial institutions. Malaysian Islamic finance global hub policy approved the market liberalization in which opened local market to foreign entities to establish companies in Malaysia.

The last literature is on the Islamic banking and financial system in Malaysia. For this topic, the researcher attempted to review previous studies that having connection with the Islamic finance global hub and available issues within the context of Islamic banking and finance in Malaysia.

1.8.1 Central Bank Supervision

There are several studies conducted by many researchers on the central bank supervision subject. James R. Barth, Luis G. Dopico, Daniel E.Nolle and James A. Wilcox[44] studied the shortcoming of the central bank supervision and found that this is due to the less reliance on market discipline as reflected in the use of sub-debt as capital and banking systems that are less likely to have explicit deposit insurance schemes.

Qiang Zhang and Gui Rong She[45] examined the implicit deposit insurance in four original state banks that undermined market discipline and created moral hazard. The differences of the degree in market discipline in different banks depend on their ownership structure as a result of varying coverage by implicit deposit insurance. This study summarized three points. Firstly, in terms of deposit growth and bank performance, different banks show differences in market discipline. Among these banks, the listed banks are the most prominent. The next are the unlisted joint-stock commercial banks and the last are the original state-owned commercial banks. Secondly, implicit deposit insurance actually undermines market discipline, which is prominent in the state-owned commercial banks. A spillover effect exists in implicit deposit insurance effect. Unlisted joint-stock commercial banks get a free ride, while listed joint-stock commercial banks do not have the spillover effect due to diversified shareholders and the stronger consciousness of the depositors.

---

[44] James R. Barth, Luis G. Dopico, Daniel E.Nolle and James A. Wilcox,"An International Comparison and Assessment of the Structure of Bank Supervision," (*Conference Paper*, February 21, 2002), 30.
[45] Qiang Zhang and Gui Rong She, "Is there any Effect of Market Discipline on China's Bank Supervision?," *Journal of Economic Policy Reform,* (Vol.11, No.1, March 2008), 29-35.

Gerald A. Mcdermott[46] examined how different political approaches to transformations shape the creation of new institutional capabilities by analyzing bank sector reforms in the 1990s in three leading post-communist democracies-Hungaries, Poland and the Czech Republic. Politicians create different political strategies that shape the organization of policymaking power, which in turn can facilitate or hinder the ability of relevant public and private actors to experiment and learn their new roles. With its emphasis on insulating power and rapidly implementing self-enforcing economic incentives, the 'depoliticization' approach creates few changes in bank behavior and indeed impedes investment in new capabilities at the bank and supervisory levels. With its emphasis on distributed authority and rules of information sharing, the 'participatory restructuring' approach appears to have fostered innovative, cost-effective monitoring structures for recapitalization, a strong supervisory system, as well as a stable and expanding banking sector.

Aneta B. Spendzharova,[47] studied the importance to have an up-dated supervision in line with the technological and product innovation as the researcher viewed the recent banks' collapse was due to this cause in partial. This study examined the regulatory power of Multi-level governance in the case of European bank regulation. As a conclusion from this study, the researcher made three propositions. Firstly, experts play essential roles in policy formulation. Indeed, the empirical analysis has shown that international experts from USAID (Untied States Agency for International Development) provided important assistance to Bulgarian supervision professionals in the period 1998-2003. World Bank and, to a lesser extent, USAID experts coached and consulted Hungarian bank supervisors in the early mid-1990s.

[46] Gerald A.McDermott, "Politics, power, and institution building: Bank crises and supervision in East Central Europe," (*Review of International Political Economy* 14:2 May 2007), 220-250.

[47] Aneta B. Spendzharova, "Multi-level Governance of Banking Regulation in the EU: Evidence from Developing Bank Supervision in Bulgaria and Hungary," (*European Integration*, Vol.32, No.3, May 2010), 249-268.

The second proposition states that public, private and international actors participate in decision-making and shape the regulatory outcomes together with national regulators. The researcher found evidence that national bank regulators in both Bulgaria and Hungary have endorsed international standards such as the Basel Accords and have effectively adopted all relevant EU banking sector legislation. Private actors especially the national peak associations of commercial banks have actively influenced this process.

Based on the third proposition, independent regulatory agencies, rather than government ministries, implement regulations and monitor compliance. In support of this proposition, the researcher views that Bulgaria's bank supervision organizationally situated within the central bank, has enjoyed significant independence from political pressure since the 1996/97 economic crisis and subsequent economic reforms. Hungary's bank supervision, situated within the overarching financial sector regulator PSZAF (the Financial Supervisory Authority in Hungary), faced challenges from the finance ministry but has asserted itself as the main public regulator in banking.

Samuel Mcphilemy[48] studied issues on a new approach undergone by the UK Financial Services Authority (FSA) before the banking crisis occurred between the years 2007-2009. The FSA presented itself as a "proportionate" and "risk based" regulator, preferring firms to adhere to the spirit of high-level principles rather than the letter of detailed rules. Simultaneously, it developed a supervisory regime that was unprecedentedly complex. This study found the degree of critical deficiencies and contradictory objectives were embedded within the FSA's 'new' approach to financial supervision from the start. Undoubtedly, the lack of intellectual challenge to efficient market thinking contributed to the FSA's failure in managing crisis that took hold from mid-2007 onwards.

[48] Samuel Mcphilemy, "Formal Rules versus Informal Relationships: Prudential Banking Supervision at the FSA Before the Crash," *New Political Economy*, (Vol.18, No.5, 2013), 748-767.

The financial crisis revealed numerous flaws and deficiencies in the FSA's risk-based supervisory framework. These failures fell within two broad categories: 'implementation gaps,' stemming from human error and problem associated with the supervisory culture; and 'system malfunctions' inherent to the design of the framework itself. With respect to the former category, an internal audit into the FSA's supervision of Northern Rock revealed numerous failures on the part of FSA staff. For example, the FSA operated an internal database, 'Interim Risk Manager,' which was designed to aggregate information about firms so that 'relationship managers' and senior staff could make judgments about the risks firms were taking. The audit revealed that the updating of this database had not been kept current, resulting in emerging risks not being elevated within FSA. Overall, this study questions the utility of the concept of regulatory capture in explaining the supervisory failures prior to the crisis.

Alexandra Hennessy[49] studied the optional decision undertaken by the European Union (EU) in the context of financial supervision either the soft or the hard law instruments. This study reflected the financial supervision changes occurred in EU from the soft co-ordination in 2009 to a banking union based on hard law in 2012/2013. This study found that to choose whether to apply hard or soft law and regulation depends on various factors. For instance, in a situation of uncertainty about high future financial risks, the governments tend to prefer soft law instruments because they value the flexibility that comes from not formalizing the provisions. Informal covenants also help prevent states member from imposing intolerable adjustment costs on one another that might be disruptive to national financial sector models. The study concludes that, the negotiations over EU financial supervision between 2009 and 2013 illustrate that the choice of soft or hard law instruments depends on the relative weight governments

[49] Alexandra Hennessy, "Redesigning Financial Supervision in the European Union," *Journal of European Public Policy*, (Vol.21, No.2, 2014), 151-168.

attach to considerations of uncertainty, national political economy models and distributive concerns.

Anichul Hoques Khan and Hasnat Dewan,[50] examined empirically the relationship between banking supervision and the instability of a banking sector. With a cross-sectional dataset from 78 countries and using a logit estimation model, the study found that the probability of instability of a country's banking sector reduces if the commercial banks are supervised exclusively by the country's central bank.

Based on the above studies, there are number of key-points could be summarized as follows:

1. Shortcoming of central bank supervision is due to less reliance on market discipline.
2. The 'participatory restructuring' approach appears to have fostered innovative, cost-effective monitoring structures for recapitalization, a strong supervisory system, and a stable, expanding banking sector.
3. In terms of deposit growth and bank performance, different banks shows differences in market discipline. Secondly, implicit deposit insurance actually undermines market discipline, which is prominent in the state-owned commercial banks.
4. Experts play an essential role in policy formulation. Then, the public, private and international actors participate in decision-making and shape the regulatory outcomes together with national regulators. Furthermore, independent regulatory agencies rather than government ministries implement regulations and monitor compliance.
5. The degree of critical deficiencies and contradictory objectives were embedded within the regulator's 'new' approach (in this case the FSA as sample) to

---

[50] Anichul Hoques Khan and Hasnat Dewan, "Who Should Supervise Banks for the Banking Sector Stability?," *Applied Economic Letters*, (Vol.20, No.17, 2013), 1531-1537.

financial supervision from the start. The lack of intellectual challenge to efficient market thinking contributed to the FSA's failure in managing crisis that took hold from mid-2007 onwards.

6. The negotiations over EU financial supervision between 2009 and 2013 illustrate that the choice of soft or hard law instruments depends on the relative weight governments attach to considerations of uncertainty, national political economy models and distributive concerns.

7. The probability of instability of a country's banking sector reduces if the commercial banks are supervised exclusively by the country's central bank.

1.9.2 Financial Liberalization

There are many studies on financial liberalization undertaken by previous researchers. Philip Arestis and Howard Stein[51] argue the financial liberalization that is implemented around the world engenders widespread financial crises precisely because of the weak foundations of its theoretical framework and poor empirical performance. Hence, the study suggested a new approach of financial liberalization, which is expected to affect financial and banking transformation, which is more consistent with the economic development. Hence, this study proposed five components namely norms, incentives, regulations, capacities and organizations. These components are the segregation of the financial system as proposed by the previous researchers. This proposal aimed at generating new forms of correlative behavior that will create a developmentally oriented financial system. According to the researchers, components, which interact originally with the ultimate objective being the generation of new common mental constructs aimed at improving coordination, generating a unity of purpose and creating greater certainty of behavior. In a financial setting, this new

[51] Philip Arestis and Howard Stein, "An Institutional Perspective to Finance and Development as an Alternative to Financial Liberalization," *International Review of Applied Economics*, (Vol.19, no.4, October 2005), 381-398.

mental constructs are vital in transforming financial systems to better serve the goals of development.

Matthew Donaghy and Michael Clarke[52] insisted the benefit of globalization in emerging Offshore Financial Centre. However, it is still under argument when it comes to sociological perspective. Hence, both researchers argued whether globalization and supposed integration of the world's OFCs has necessarily eroded local process. The researchers provide sample on Switzerland where transformation in the rules relating to bank confidentially, which appeared to have rendered its financial centers, are more homogenous with other centers, has not eroded the historically constituted psyche and has an institutional framework conducive to monetary privacy. According to the researchers, international financial markets may indeed be global in their range, but they operate through local financial centers, both the Offshore Financial Centres (OFCs) and nation state.

David R. Meyer [53] studied job mobility of investments bankers that operates in a "small world" and organized around banks in global financial centers. This study found that inter-city job changes involving London and New York with Hong Kong occurred through intra-organizational job changes, not inter-city inter-organizational moves. This is evidenced through the experience by eight leading investment bankers, which were the samples of the current study. The job mobility of those who worked at Citygroup in Hong Kong, at some point in their career, reveals that local networks, either cohesive or have weak ties, provide smooth paths for job mobility among firms.

[52] Metthew Donaghy and Michael Clarke, "Multi-Level Governance of Banking Regulation in the EU: Evidence from Developing Bank Supervision in Bulgaria and Hungary," *European Integration*, (Vol.32, No.3, May 2010), 249-268.
[53] David R.Meyer, "Small-World job Mobility Integrates Hong Kong with Global Financial Centers," *Asian Geographer*, (Vol.28, No. 1, June 2011), 51-63.

Anindya K. Bhattacharya[54] examined the feasibility of establishing an international financial center in Shanghai by 2020. The study analyzed the financial liberalization market measures undertaken so far by China that meets the requirements for the success of this strategy. This study concluded that elevating Shanghai to primary international financial services to domestic and foreign clients is decades away under the sequential approach to liberalization. However, in the short run, Shanghai can emerge as a regional financial center catering essentially to the funding needs of Chinese business.

Ewald Engelen and Anna Glasmacher[55] investigated, first, the extent to which urban boosters are deliberately pursuing financial strategies through the internet, and second, how their negotiations of the global and the local, space and place, the universal and the particular, modernity and tradition result in "multiple modernities," as projected through the imaginaries on International Financial Centers websites. The conclusions that can be drawn from this analysis consist of four ideas. First, size matters. The effort that urban boosters put into Internet representations is affected by the size and status of an IFC. The larger, more uncontested and well-established the IFC, the less importance is attached to its marketing through the Internet. Second, history matters. A historical pedigree is a cultural resource that suggests reliability, expertise, the existence of networks and trustworthiness. Third, regulatory status has become a tool of competition. While this was seen as driving a race to the bottom before the crisis, since the G20 meeting in London of April 2009, the direction of competition has hesitantly been reversed. The coordinated backlash against uncooperative tax havens has resulted in defensive measures by well-known off-shore centres. The political nature of this back-lash is evident from the absence of any re-regulatory drive against mainstream IFCs

[54] Anindya K. Bhattacharya. "The Feasibility of Establishing an International Financial Center in Shanghai," *Journal of Asia-Pacific Business*, (12, 2011), 123-140.

[55] Ewald Engelen and Anna Glasmacher, "Multiple Financial Modernities, International Financial Centers, Urban Boosters and the Internet as the Site of Negotiations," *Regional Studies*, (Vol. 47, No.6, 2013), 850-867.

such London and Amsterdam which pursue largely the same strategy as self-defensive and often criticized ‘villains’ such as Luxembourg and the Cayman Islands. Fourth, the analysis suggests that the cultural idiom of modernization in finance is increasingly hybridizing, but still heavily influenced by “western way” of performing finance. Both, in terms of visual imagery (colorings and architecture) and representation of socio-political associations (Islamic finance and references to political rulers), the IFCs from Asia and the Middle East project a “vernacular modernity” that is both universal and site specific.

Based on the above study, there are number of key-points could be summarized as follows:

1. There are five components of financial settings proposed as a new mental constructs in transforming financial systems namely; norms, incentives, regulations, capacities and organizations.
2. International financial markets may indeed be global in their range, but they operate through local financial centers, both Offshore Financial Centres (OFCs) and nation state.
3. The job mobility of those who worked at Citygroup for instance in Hong Kong at some point in their career reveals that local networks either cohesive or weak ties, provide smooth paths for job mobility among firms.
4. In a specific study on Shanghai, elevating the area to a primary international financial services to domestic and foreign clients is decades away under the sequential approach to liberalization. However, in the short run, Shanghai can emerge as a regional financial center.
5. The extent to which urban boosters are deliberately pursuing financial strategies through the internet, and how their negotiations of the global and the local, space and place, the universal and the particular, modernity and tradition result in

"multiple modernities," Conclusion can be drawn to consist of fourfold. First; size matter, second; history matter, third; regulatory status fourth; cultural idiom of modernization in finance.

1.9.3 Global Islamic Finance

M. Mansoor Khan, M. Ishaq Bhatti[56] studied the appearance of Islamic finance as an alternative to the conventional financial systems, which has been applied in many countries around the world such as in Middle East countries, South-Asia, South-East Asia, Africa as well as in Europe and Western countries. This study observed current development of Islamic finance in many countries globally and found that Islamic finance industry could emerge as an alternative to the conventional financial system counterpart. Among the factors contributing to the development of Islamic finance systems are the hiking of oil prices, the economic sustainable in the Middle-East, product development and innovation, receptive attitude of conventional regulators, the advancement of information technology that becomes as catalyst for Islamic finance to go global.

Ayman Zerban, Eslam H. Elkady and Rafik F. Omar[57] observed the recent financial crisis causes and attempted to propose an Islamic financial system as an alternative solution for the financial crisis. This study observed the Islamic finance system, which consists of Islamic finance principles, issues and a comparative study on Islamic finance and the conventional counterpart. The study concluded that the Islamic finance, which is based on *Sharī'ah* ruling is the divine rule by the Almighty for human prosperity and welfare. Although some pitfall may happen along the way in implementing the system, for instance in some Islamic finance products, it opens a door

[56] M. Mansoor Khan, M. Ishaq Bhatti, "Islamic banking and finance: On its way to globalization," *Emerald Journal, Emerald Group Publishing Limited*, (Vol.34, No. 10., 2008).

[57] Ayman Zerban, Eslam H. Elkady and Rafik F. Omar, (2012), Islamic Finance and Global Financial Crises: How To keep Finance on Track, Topics in Middle Eastern and North African Economies," *Electronic Journal, Middle East Economic Association and Loyola University Chicago*, (Vol.14, September , 2012).

for more accurate procedure by the authorities and other related parties to strengthen the system through new regulations and guidelines.

R. Ibrahim Adebayo and M. Kabir Hassan[58] studied the ethical principles in Islamic financial institutions. The researchers insist the impotency of ethics in a financial system to eliminate misconduct in dealing with funds. Until some extend, the conventional system also attempts to adopt the philosophy of ethics in their financial system as evidenced from the launching of Sabrane Oxly Act in 2002 in America. In this act, several terms and conditions were dedicated to ensure a safe financial system. However, the imposition of several conditions has influenced customers' perception, which is far from the current practice. Hence, this adjustment must come with the spirit of religion, as every Muslim understands that the application of a true Islamic financial system is a requirement for them. In conclusion, this study found that the ethical principles of Islamic financial institutions cannot be compromised as it is their divine origin. Hence, for an Islamic financial system to become viable alternative to the conventional economic system, the ethical factor that drives the system must be upheld.

Muhammad Hanif[59] studied the perceptional issues on the similarities and differences in Islamic banking and conventional banking. The researcher made several comparative studies on certain instruments of the banking system such deposits, short-term loans, medium- to long-term loans, leasing, agricultural loans, house financing and investments. This study found that the Islamic finance system is a system that stands alone and not merely adopting the conventional system as perceived by some scholars. The system of Islamic finance consists of *Sharī'ah* screening board, *Sharī'ah* Advisory and is based on Islamic rulings, which is named as *Sharī'ah*. The Islamic financial

---

[58] R. Ibrahim Adebayo and M. Kabir Hassan (2013), "Ethical Principles of Islamic Financial Institutions," *Journal of Economic Cooperation and Development*, (Vol. 34. No.1, Turkey: Statistical Economic and Social Research and Training Centre for Islamic Countries, 2013), 63-90.

[59] Muhammad Hanif, "Differences and Similarities in Islamic and Conventional Banking," *Journal of Business and Social Sciences*, (Vol. 2, No.2, February 2011).

system also eliminates all prohibited elements like *riba* (usury), *gharar* (uncertainty), *maysir* (gambling) and other elements of the same nature.

Frederick V.Perry, J.D and Scheherazade S. Rehman[60] studied the globalization of Islamic finance that focus on many aspects of globalization. Among others, issues with regard to the increase of acceptability of Islamic finance in the European countries, Islamic jurisprudence, global standards and integration of Islamic finance. This study concluded that in the near term, Islamic finance might not appear to be a globally accepted financial system. This is based on the requirement to fully convert the financial system in Islamic countries into the Islamic financial system.

Some economist claims that the recent financial crisis, so called sub-prime, had given an opportunity for Islamic finance to appear as an alternative financial system. However, the researcher argues that the exposure for the same risk yet to be reached in Islamic finance and the same result is assumed for Islamic finance in the event of over financing on the housing finance.

Furthermore, the system of Islamic finance merely provides financial services and product, which reflect a small segment of the financial system. Thus, it could not become as a universal system, which consists of more complex system. Yet, it remains as a niche market and for the time being as an alternative.

Mercy A.Kuo[61] studied the strategic link between Middle East petrodollar investors and the Asian Banks in influencing the development of Islamic banking and finance in Southeast Asia. This study in particular examined the growth of Islamic finance in Southeast Asia countries such as Malaysia and Singapore. This study ended with a discussion on the global financial issues and the importance for the Islamic finance industry to absorb the risk by strategizing certain measures such as

---

[60] Frederick V.Perry, J.D and Scheherazade S. Rehman, "Globalization of Islamic Finance: Myth or Reality?" *Journal of Humanities and Social Science*, (Vol.1 No.9; December 2011).

[61] Mercy A. Kuo, "Islamic Finance in Southeast Asia: Strategic Context and Trends," *Journal of Islamic Economics, Banking and Finance, (JIEBF),* (Vol. 5, No.3, September – December 2009, Bangladesh: Islami Bank and Training and Research Academy (IBTRA)).

strengthening management system, enhancing regulatory structure to be in line with the authoritative standard bodies like IFSB= Islamic Finance Services Board and AAOIFI=Accounting and Auditing Organization for Islamic Financial Services as well as encouraging financial innovation and Islamic Capital market development. To ensure the bright future of Islamic finance, a comprehensive training and education must be implemented in order to produce a well-talented human capital in Islamic finance.

Wafica Ali Ghoul,[62] examined the financial crisis which effects the Islamic finance sector by taking lessons from the conventional financial experience. This study focused as well on the role played by the *Sharī'ah* scholar in managing the *Sharī'ah* risk. This study arrived at a conclusion that for the future development of new Islamic product, it must be based on pure *Sharī'ah* element without adoption from the conventional products.

Ahmet Selçuk DİZKIRICI[63] studied the opportunity for Istanbul to become a financial center based on its specialty as a Eurasia country. In the beginning, this study discussed the meaning of financial center and its description in general and further highlighted the positive factors of Istanbul to become a financial centre. In the economic scale, Turkish's economy is Europe's 6th and the world's 16th biggest economy as reported in 2011 GDP. Turkey's strategic location attracts investors from both Western and Asian countries to invest in the country. The researcher, in the end, proposed some measures to be taken by the authorities such as transforming Istanbul into a center of "interest free financing," "private equity" and "carbon finance," in Eurasia as a regional financial centre. The collaboration effort between the government and private entities is important to ensure economic stability and more efforts are required to develop

[62] Wafica Ali Ghoul, "The Dilemma Facing Islamic Finance and Lessons Learned from the Global Financial Crisis," *Journal of Islamic Economics, Banking and Finance, (JIEBF)*, (Vol. 7, No.1, January – March 2011, Islami Bank and Training and Research Academy (IBTRA), Bangladesh (2011)).
[63] Ahmet Selçuk DİZKIRICI, (2012), "Considering Istanbul As A Financial Center: Targets, Following Steps," *Journal of Business and Social Science*, (Vol.3 No. 18, (Special Issue-September 2012)).

advanced infrastructure, to produce a high skill of human capitals, to promote an attractive tax charges, and to establish a fair legislation.

Based on the above studies, there are number of main points could be concluded as follows:

1. Islamic finance industry could emerge as an alternative to the conventional financial system counterpart. Among the factors contributing to the development of Islamic finance systems are the hiking of oil prices, the economic sustainable in the middle-east, product development and innovation, receptive attitude of conventional regulators, the advancement of information technology that becomes as catalyst for Islamic finance to go global.
2. The Islamic finance which is based on the *Sharī'ah* ruling is the divine rule by the almighty for human prosperity and welfare.
3. The ethical principles of Islamic financial institutions cannot be compromised as it is their divine origin. Hence, for Islamic financial system to become a viable alternative to the conventional economic system, the ethical factor driving the system must be upheld.
4. The Islamic finance system is a system which stands alone and not merely adopting the conventional system as perceived by some scholars.
5. In the near term, Islamic finance is unlikely to appear as a globally accepted financial system. This is based on the requirement to fully convert the financial system in Islamic countries into the Islamic financial system.
6. The importance for Islamic finance industry to absorb the risk by strategizing certain measures such strengthening management system and enhancing regulatory structure to be in line with the authoritative standard bodies like IFSB and AAOIFI.

7. For the future development of new Islamic products, it must be based on pure *Sharī'ah* element without adoption from the conventional products.
8. The collaborative effort between the government and private entities is important to ensure economic stability and more efforts are required to develop advanced infrastructure, to produce a high skill of human capitals, to promote an attractive tax charges, and to establish a fair legislation and many more.

1.9.4 Empirical Study

Fatma Zehri and Najya AL-HERCH[64] studied the impact of global financial crisis towards Islamic Banks with the comparison to the conventional banks based on accounting ratios. The researchers used 26 financial ratios in the Stepwise Logit model to scrutinize the probability to differentiate between both banks in the international context relying on financial characteristics.

The rationale of using the accounting ratio as a measurement demonstrates the reliability of the method in the banking observation for over 110 years. This method could be applied in distinguishing IBs and CBs in the international context. The researchers also proposed a new variable in determining the impact of global financial crisis against IBs with a comparison to CBs, named as CRISIS, which elaborately is a time measurement to distinguish between the crisis period and pre-crisis period. Based on the Logit analysis, the result shows that IBs is more stable and sustainable during the global financial crisis in 2007-2008 periods, which indicates the effectiveness of *Sharī'ah* factor as influence.

Julius B. Bertillo, Josefina B. Salindo and Florabel O. Nieva[65] studied the global impact of financial systems in the Arab World. The aim of this research was to observe

[64] Fatma Zehri and Najya AL-HERCH, "The Impact of the Global Financial Crisis On The Financial Institutions: A Comparison Between Islamic Canks (IBs) and Conventional Banks (Cbs)," *Journal of Islamic Economics, Banking and Finance (JIEBF)*, (Vol.9, No.3, July-September 2013).

[65] Julius B. Bertillo, Josefina B. Salindo and Florabel O. Nieva, (2013), "Global Impact of Financial Systems in the Arab World," *Sosial Science and Research Network*, Available at: "http://papers.ssrn.com/sol3/papers. cfm?abstract_id=2287415."

the global financial system in the Arab world with more focus on the Islamic finance systems: principles and prohibitions; traditions and practices; and challenges and opportunities in the Arab world. As Islamic finance is a system that prohibits elements of *gharar* (uncertainty), *riba* (usury), *maysir* (gambling) and other elements that are considered unlawful as stated in the *Quran* and *Hadith*. Thus, the basic principle of Islamic finance is based on profit and loss sharing. In the Arab communities, Islamic finance system has been practiced since a long time ago.

Based on the findings, this research concluded that the Arab world's practices Islamic finance without interest and applies profit and loss sharing in their financial systems. Further, the Islamic finance systems also consists of risk management, fairness, avoidance of uncertainty, prohibition of gambling and constructed based on the *Sharī'ah* law. Islamic financial institutions in the GCC (Gulf Cooperation Council) become the prime source of capital and contribute to the growth of Islamic finance globally.

Rashidah Abdul Rahman, Siti Balqis and Faizal Dean[66] assessed risk management practices in a comparative study between Pakistan and Malaysia. The risk management consists of risk management, risk identification, risk assessment and analysis as well as risk monitoring. This study found that risk identification and risk assessment and analysis are the most influencing factors in risk management practices in both countries. The result also shows that both countries are very efficient in managing risk.

Yap Voon Choong, Chan Kok Thim and Bermet Talasbek Kyzy[67] analyzed the most important indicators of bank performance. This study used a regression model

[66] Rashidah Abdul Rahman, Siti Balqis and Faizal Dean, "Assessing the Risk Management Practices of Islamic Banks: Empirical Evidence from Malaysia and Pakistan," *Journal of Islamic Economics, Banking and Finance (JIEBF),* (Vol.9, No.4, October-December 2013).

[67] Yap Voon Choong, Chan Kok Thim and Bermet Talasbek Kyzy, "Performance of Islamic Commercial Banks in Malaysia: An Empirical Study," *Journal of Islamic Economics, Banking and Finance (JIEBF),* (Vol.8, No.2, April-June 2012).

consists of dependent variables (ROA and ROE) and numerous independent variables to analyze the performance of Islamic commercial banks. The empirical result shows that credit risk is the most significant performance indicator of Malaysia's Islamic commercial banks. The other factors of significant importance are liquidity rate and concentration of Islamic commercial banking.

Shaista Wasiuzzaman and Hanimas-Ayu Bt Ahmad Tarmizi[68] examined how bank's characteristic and macroeconomic factors influenced the profitability of Islamic banks in Malaysia. This study employed Ordinary Least Squares (OLS) method to analyze the data collected from 16 Islamic banks/windows. Specifically, bank's determinants are such as liquidity, capitalization, asset quality and operational efficiency were used to regress against profitability. This study also took into account macroeconomic factors such as gross domestic products and inflation in analyzing the impact towards Islamic banks. The test shows that capital, liquidity, operational efficiency, asset quality, gross domestic product (GDP) and inflation affect profitability of Islamic banks in Malaysia. Based on the regression model, the profits generated by Islamic banks have a positive relationship with the liquidity and the macroeconomic environment, but are negatively related to the asset quality and capital. This result indicates that policies applied in controlling inflation rate and the GDP growth should become a prime concern in strengthening financial intermediation.

In conclusion, based on the findings of past studies, a real issue emerges in three main topics. In Central banking supervision, the issues are about the control power by the central bank towards local banks. These literatures prove the roles of the central bank in controlling and supervising local banks through the application of certain regulations. Simultaneously, the central bank plays a role in designing future pathway of the banking system in the country. In relation to this thesis, the Central Bank of

---

[68] Shaista Wasiuzzaman and Hanimas-Ayu Bt Ahmad Tarmizi, Profitability of Islamic Banks in Malaysia: An Empirical Analysis," *Journal of Islamic Economics, Banking and Finance*, (Vol.6, No.4, October-December 2010).

Malaysia as bank's regulator plays a vital role in visioning the Islamic finance global hub idea. Hence, a clear objective of the future development of Islamic banking and finance in Malaysia was drawn to achieve the Islamic finance global hub target. This objective is equal to positioning the country as a financial center in the conventional perspective.

Observing literatures on financial liberalization benefits this study in terms of the historical practice of liberalization and the negative and positive impacts from this policy. The Central Bank of Malaysia has clearly stated in its first plan of their Financial Sector Masterplan (2000-2010) to liberalize the Islamic financial services within that period. This study is important to ensure that the country has made sufficient preparation to leap into the liberalization era. Therefore, it is imperative to have adequate understanding on issues such as the competitiveness of local Islamic Financial Institutions (IFIs) and the competition among the IFIs and other related issues, which are part of the current study.

Reviewing Islamic banking and finance literatures reflects a wide issue of Islamic banking and finance, especially in Malaysia. The review of previous studies shows that there is yet a research being conducted on Islamic finance global hub theoretically and empirically. However, some studies have relations with the issue of globalization as studied by Julius B. Bertillo, Josefina B. Salindo and Florabel O. Nieva[69], which the study was on the global impact of financial systems in the Arab World.

Based on the above study, there are number of main points could be concluded as follows:

[69] Julius B. Bertillo, Josefina B. Salindo and Florabel O. Nieva, (2013), "Global Impact of Financial Systems in the Arab World," *Sosial Science and Research Network*, Available at: "http://papers.ssrn.com/sol3/papers. cfm?abstract_id=2287415."

1. Based on a Logit analysis, the result shows that IBs is more stable and sustainable during the global financial crisis in 2007-2008 periods, which indicates the effectiveness of *Sharī'ah* factor as influence.
2. The Arab world's practices Islamic finance without interest and applies profit and loss sharing in their financial systems.
3. The risk identification and risk assessment and analysis are the most influencing factors in risk management practices in Malaysia and Pakistan. The result also shows that both countries are very efficient in managing risk.
4. The credit risk is the most significant performance indicator of Malaysia's Islamic commercial banks. Other factors are liquidity rate and concentration of Islamic commercial banking.
5. The study shows that capital, liquidity, operational efficiency, asset quality, gross domestic product (GDP) and inflation affect profitability of Islamic banks in Malaysia.

A combination of these three main topics in this literature contributes a complete understanding of this study.

Table 1.6: The following table consists of the details of the literature review:

Author	Focus/Issues	Method(s) of Analysis	Main Finding(s)
Central Bank Supervision			
James R. Barth, Luis G. Dopico, Daniel E.Nolle and James A. Wilcox (2002)	Shortcoming of central bank supervision	Conceptual Study	Less reliance on market discipline caused shortcomings in the banking system.
Gerald A. Mcdermott (2007)	Examines how different political approaches to transformations shape the creation of new institutional capabilities by analyzing bank sector reforms in the 1990s in three leading post-communist	Conceptual Study	The 'participatory restructuring' approach appears to have fostered innovative, cost-effective monitoring structures for recapitalization, a strong supervisory system, and a stable, expanding banking sector.

	democracies-Hungaries, Poland and the Czech Republic.		
Qiang Zhang and Gui Rong She (2008)	Examine the implicit deposit insurance in the four original state banks, undermines market discipline and creates moral hazard.	Demirgūç-Kunt and Huizinga method	Firstly, in terms of deposit growth and bank performance, different banks shows differences in market discipline. Secondly, implicit deposit insurance actually undermines market discipline, which is prominent in the state-owned commercial banks.
Aneta B. Spendzharova (2010)	The recent banks collapse is due to insufficient technology.	Conceptual Study	First proposition: experts play an essential role in policy formulation. The second proposition stipulates that public, private and international actors participate in decision-making and shape the regulatory outcomes together with national regulators. The third proposition states that independent regulatory agencies rather than government ministries, implement regulations and monitor compliance.
Samuel Mcphilemy (2013)	To a new approach undergone by the UK Financial Services Authority (FSA) before the banking crisis occurred between 2007-2009.	Conceptual Study	This study found the degree of critical deficiencies and contradictory objectives were embedded within the FSA's 'new' approach to financial supervision from the start. The lack of intellectual challenge to efficient market thinking contributed to the FSA's failure in managing crisis that took hold from

			mid-2007 onwards.
Alexandra Hennessy (2014)	Optional decision undertaken by the European Union (EU) in the context of financial supervision either the soft or the hard law instruments.	Conceptual Study	The study concludes that, the negotiations over EU financial supervision between 2009 and 2013 illustrate that the choice of soft or hard law instruments depends on the relative weight governments attach to considerations of uncertainty, national political economy models and distributive concerns.
Anichul Hoques Khan and Hasnat Dewan (2013)	Examines empirically the relationship between banking supervision and the instability of a banking sector.	Logit Model	The study found that the probability of instability of a country's banking sector reduces if the commercial banks are supervised exclusively by the country's central bank.
Financial liberalization			
Philip Arestis and Howard Stein (2005)	Financial liberalization that is implemented around the world engenders widespread financial crises precisely because of the weak foundations of its theoretical framework and poor empirical performance.	Conceptual Study	This study proposed five components namely; norms, incentives, regulations, capacities and organizations. In a financial setting, this new mental constructs are vital in transforming financial systems to better serve the goals of development.
Matthew Donaghy and Michael Clarke (2010)	Globalization and supposed integration of the world's OFCs has necessarily eroded local process.	Conceptual Study	According to the researchers, international financial markets may indeed be global in their range, but they operate through local financial centers, both Offshore Financial Centres (OFCs) and nation

			state.
David R. Meyer (2011)	Studied job mobility of investments bankers operates in a "small world," organized around banks in global financial centers.	Conceptual	The job mobility of those who worked at Citygroup in Hong Kong at some point in their career reveals that local networks either cohesive or weak ties, provide smooth paths for job mobility among firms.
Anindya K. Bhattacharya (2011)	Examines the feasibility of establishing an international financial center in Shanghai by 2020.	Conceptual Study	This study concludes that elevating Shanghai to a primary international financial services to domestic and foreign clients is decades away under the sequential approach to liberalization. However, in the short run, Shanghai can emerge as a regional financial center
Ewald Engelen and Anna Glasmacher (2013)	Investigates, first, the extent to which urban boosters are deliberately pursuing financial strategies through the internet, and second, how their negotiations of the global and the local, space and place, the universal and the particular, modernity and tradition result in "multiple modernities,"	Conceptual Study	Conclusion can be drawn to consist of fourfold. First; size matter, second; history matter, third; regulatory status fourth; cultural idiom of modernization in finance.
Global Islamic Finance			
M. Mansoor Khan, M. Ishaq Bhatti (2008)	Studied the appearance of Islamic finance as alternative to the conventional financial systems which has been applied in many countries around the world such in middle East	Conceptual Study	Islamic finance industry could emerge as an alternative to the conventional financial system counterpart. Among the factors contributing to the development of Islamic finance

	countries, in south-Asia, in South-East Asia, in Africa and not least in Europe and western countries.		systems are the hiking of oil prices, the economic sustainable in the middle-east, product development and innovation, receptive attitude of conventional regulators, the advancement of information technology that becomes as catalyst for Islamic finance to go global.
Ayman Zerban, Eslam H. Elkady and Rafik F. Omar (2012)	Observed the recent financial crisis causes and attempts to propose Islamic financial system as an alternative solution for the financial crisis.	Conceptual Study	The study concluded that the Islamic finance which is based on the *Sharīʼah* ruling is the divine rule by the almighty for human prosperity and welfare
R. Ibrahim Adebayo and M. Kabir Hassan (2013)	Studied on the ethical principles in Islamic financial institutions.	Conceptual Study	This study found that the ethical principles of Islamic financial institutions cannot be compromised as it is their divine origin. Hence, for Islamic financial system to become a viable alternative to the conventional economic system, the ethical factor driving the system must be upheld.
Muhammad Hanif (2011)	Studied the perceptional issues on the similarities and differences in Islamic and conventional banking.	Conceptual Study	The Islamic finance system is a system which stands alone and not merely adopting the conventional system as perceived by some scholars.
Frederick V.Perry, J.D and Scheherazade S. Rehman (2011)	Studied the globalization of Islamic finance with the focus on many aspects of globalization.	Conceptual Study	In the near term, Islamic finance is unlikely to appear as a globally accepted financial system. This is based on the requirement to fully convert the financial

			system in Islamic countries into the Islamic financial system.
Mercy A.Kuo (2009)	The strategic link between Middle East petrodollar investors and the Asian Banks in influencing the development of Islamic banking and finance in Southeast Asia.	Conceptual Study	The importance for Islamic finance industry to absorb the risk by strategizing certain measures such strengthening management system and enhancing regulatory structure to be in line with the authoritative standard bodies like IFSB and AAOIFI.
Wafica Ali Ghoul (2011)	Financial crisis which affects the Islamic finance sector by taking lessons from the conventional financial experience.	Conceptual Study	For the future development of new Islamic products, it must be based on pure *Sharī'ah* element without adoption from the conventional products.
Ahmet Selçuk DİZKIRICI (2012)	The opportunity of Istanbul to become a financial center based on its specialty as a Eurasian country.	Conceptual Study	The collaborative effort between the government and private entities is important to ensure economic stability and more efforts are required to develop advanced infrastructure, to produce a high skill of human capitals, to promote an attractive tax charges, and to establish a fair legislation and many more.
Empirical Study			
Fatma Zehri and Najya AL-HERCH (2013)	Impact of global financial crisis towards Islamic Banks with a comparison to the conventional banks based on accounting ratios.	Logit Analysis	Based on a Logit analysis, the result shows that IBs is more stable and sustainable during the global financial crisis in 2007-2008 periods, which indicates the effectiveness of *Sharī'ah* factor as influence.

Julius B. Bertillo, Josefina B. Salindo and Florabel O. Nieva (2013)	A study on the global impact of financial systems in the Arab World. The aim of this research was to observe the global financial system in the Arab world with more focus on the Islamic finance systems: principles and prohibitions: traditions and practices; and challenges and opportunities in the Arab world.	Descriptive Analysis	This research concluded that the Arab world's practices Islamic finance without interest and applies profit and loss sharing in their financial systems.
Rashidah Abdul Rahman, Siti Balqis and Faizal Dean (2013)	Assessed the risk management practices in a comparative study between Pakistan and Malaysia.	Descriptive Analysis	The risk identification and risk assessment and analysis are the most influencing factors in risk management practices in both countries. The result also shows that both countries are very efficient in managing risk.
Yap Voon Choong, Chan Kok Thim and Bermet Talasbek Kyzy (2012)	Analyzed indicators of bank performance with a specific aim to determine the most important indicator of bank performance.	Regression Analysis	The credit risk is the most significant performance indicator of Malaysia's Islamic commercial banks. Other factors are liquidity rate and concentration of Islamic commercial banking.
Shaista Wasiuzzaman and Hanimas-Ayu Bt Ahmad Tarmizi,(2010)	Examined how the bank's characteristics and macroeconomic factors influenced the profitability of Islamic banks in Malaysia.	Ordinary Least Squares	The study shows that capital, liquidity, operational efficiency, asset quality, gross domestic product (GDP) and inflation affect profitability of Islamic banks in Malaysia.

1.10 RESEARCH FRAMEWORK

This thesis is divided into seven chapters. The first chapter is a complete description of how the study was conducted to serve as a guide (roadmap) in doing research. This chapter provides the introduction of the study including the research background, problem statement, research objective, research significant, literature reviews and research framework.

Chapter two discusses the framework of Islamic finance as practiced in Malaysia. Further information regarding to the Islamic financial system, which consists of Islamic banking, *Takaful* and Islamic Capital market are discussed in depth to build a better understanding of the system.

Chapter three presents a thorough analysis of the Islamic finance global hub concept. This chapter starts with the definition of financial centre and then discusses the type and category of financial internalization transformation process. The financial internationalization process has a staggered development starting from Multinational Banking Offshore, followed by Financial Center, then International Financial Center and finally to the Global Financial Centre.

This chapter also presents the outcome of the examination of the impact of globalization towards Islamic finance and the possibility of the Islamic finance to be involved in the financial liberalization agenda. This chapter also presents the findings on Malaysia's experience in liberalizing its financial sector with more focus on the liberalization of Malaysia's Islamic finance comprises Islamic banking, *Takaful* and Islamic capital market. Finally, this chapter presents the established understanding of the definition of the financial centre and the possibility of Islamic finance to participate in the system with the details of Malaysia's experience in Islamic finance liberalization.

Chapter four presents a study on the initiatives undertaken by the Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic finance. The Central

Bank of Malaysia has taken pertinent effort in developing Islamic Finance in Malaysia and further with a vision to position Malaysia as a global hub for Islamic finance. Among the measures taken by the Central Bank of Malaysia in strengthening Malaysia's Islamic finance are strengthening the Regulatory Policy and Supporting Frameworks, the Establishment of the Financial Sector Master Plan (FSMP), the Establishment of Malaysia International Islamic Financial Centre (MIFC), Malaysia's Government Support: Tax Incentives, strengthening *Sharī'ah* Factors and developing The Centre For Human Capital Development in Islamic Finance. This Chapter finally present reviews on Malaysia's position among the global Islamic finance countries worldwide.

Chapter five is the most important chapter due to its critical analysis on issues pertaining to the challenges and issues emerge in the path to positioning Malaysia as the Islamic finance global hub country. This chapter examines five issues namely; 1) Analysis on the Central Bank of Malaysia's Initiative and the Government Supportive Factors in Promoting Malaysia as an Islamic Finance Global Hub, 2) Analysis on the Requirement for the Establishment of Islamic Finance Court, 3) Competition Between Local and Foreign Islamic Financial Institutions, 4) The Internationalization of Local Islamic Finance Institutions, 5) Mega Islamic Bank and 6) Human Capital Issues in Islamic Finance. In order to verify the issue, an interview method was used to seek personal views and experience from Islamic finance scholars, regulators and practitioners.

Chapter six examines the assessment bodies doing assessment on the performance of global financial center. The prime objective of this assessment was to make a comparative analysis among the bodies on available methods used in their assessment, which are useful in establishing a new Islamic finance global hub index. This study eventually proposes a framework for Islamic finance global hub index. This framework then was verified through a survey and interview methods, which further validate the reliability of the index.

Chapter seven consists of the conclusion and a proposal which proposes several measures of Islamic finance authorities especially the Central Bank of Malaysia as a regulator in Malaysia in order to manage the determined challenges. This chapter also provides recommendations and method of assessment in measuring Islamic finance global hub countries.

CHAPTER TWO

MALAYSIA’S ISLAMIC FINANCE FRAMEWORK

2.0 INTRODUCTION TO THE ISLAMIC ECONOMICS AND FINANCE

This chapter attempts to answer the first question as highlighted in the problem statement in the first chapter. The ample information on Malaysia’s Islamic finance framework will guide this study into a correct scope of study.

Basically, the word economics suggests a study of man’s behavior as agents of consumption and production. The most essential factor, which ascertains man’s conduct, is the system of values he exercises or contributes to. As such it is impossible to propose an authentic picture of man’s behavior without providing due to honor the value system he offers to.[70]

The existence of Islamic economics is verified through Surah *al-Māidah*, where Allah S.W.T says:

ٱلْيَوْمَ أَكْمَلْتُ لَكُمْ دِينَكُمْ وَأَتْمَمْتُ عَلَيْكُمْ نِعْمَتِي وَرَضِيتُ لَكُمُ ٱلْإِسْلَٰمَ دِينًا

(*al- Māidah* 5:3)

> Translation: …This day I have perfected your religion for you and completed my favour to you, and I have chosen Islam to be your faith…..[71]

Based on the above verse, Islam clearly comprises all aspects of human life such as social prosperity law and regulations, behavior, worship, relationship between human beings, family harmonization rules as well as economic and finance.

---

[70] Syed Othman al-Habshi, et.al, *An Introduction to Islamic Economics and Finance*, (Kuala Lumpur: CERT
Publication Sdn. Bhd., 2011), 31.

[71] Department of Islamic Development Malaysia, Tafsir ar-Rahman Interpretation of the Meaning of the Quran, (Putrajaya, Malaysia: Department of Islamic Development Malaysia, 2007), 182.

Islamic norms and values surpass locality and time boundaries, cultural as well as racial barriers. The sphere of economics cannot escape the influence of such comprehensive
values. It cannot, therefore, exit the Islamic norms to investigate conventional economics.[72]

Islamic understanding on economic differs than other economic concepts either capitalist or socialist. Islam emphasizes moral values in its economic concept, which promotes justice and fairness. In Islam, everything in this world belongs to Allah. In all sense, this is the thought of ownership in Islam in which human behaves as a trustee and is obliged over any conduct. Economic doctrine in Islam is based on mutual cooperation and accountability, which from this will establish a good individual behavior like responsibility and honesty.[73]

Since finance is a part of the economic system, hence, Islamic finance is a part of Islamic Economics. Finance is about money matters. The phrase "Islamic Finance," implies two important points. The noun "finance," proposes that Islamic financial markets and institutions deal with resource apportionment management, acquisition and investment. It also deals with the fundamental issue in finance, which is risk transformation and management.

Hence, Islamic finance is likely to essentially operate likewise or at least brings forth the same economic effect to that of its conventional counterpart. Nevertheless the adjective "Islamic" suggests a little fundamental difference between Islamic finance and its conventional counterpart. Certainly, Islamic finance is formed upon some special and unique characteristics, which are based on certain *Sharī'ah* rules.

---

[72] *Ibid*.

[73] Kamal Khir, Lokesh Gupta and Bala Shanmugan, *Islamic Banking: A Practical Perspective*, (Selangor: Pearson Malaysia Sdn. Bhd. 2009), 7.

Some of the prominent principles comprising parts of it include: the forbiddance of *riba* or pre-determined rate of interest, the impediment of *gharar* (ambiguity) in contracts, the prohibition of unjust and unfair economic activities and unethical behavior such as pornography, gambling, alcohol and prostitution. Hence, Islam promotes the harmonization of socioeconomic activities such as the introduction of a religious levy or alms giving (*zakat*) and co-operation for the benefit of the society and the development of all legitimized (*halal*) aspects of business trades and investments.[74]

2.1 ISLAMIC ECONOMIC PRINCIPLES

There are three main features of the economic system, which are usually referred to as the major distinguishing elements of any economic system.

2.1.1Private Ownership and Property

In Islam, property is a trust and human is a mere owner of the property while Allah is the real owner. The use of property by human is based on the limitation as specified by Allah S.W.T in which human acts as a trustee or viceroy. The right to use property is not definite. Hence, the code of conduct in using property is based on the common good and the welfare of Muslims and assigned in the decision-making process of every Muslim.[75]

Islam permits private ownership of property as long as the rules associated with the trust are not violated. There are also protections exercised against the predatory acts to secure the ownership by the individuals or groups of individuals and also the state. If there are wider interests of the community demand, the State may acquire private property from individuals but only after paying a fair compensation as agreed by both parties. The right to acquire private ownership is based on a person's capacity to utilize it fully and to manage it properly. For instance, if a piece of cultivable land is not

[74] International Shari'ah Research Academy for Islamic Finance (ISRA), Islamic Financial System: Principles and Operations, (Kuala Lumpur: International Sharia'h Research Academy for Islamic Finance, 2011). 5.

[75] Mian M. Nazeer, *The Islamic Economic System: A Few Highlights*, (Islamabad: Pakistan Institute of Development Economic Order, 1981), 28.

utilized for three consecutive years, the government has the right to forfeit the private ownership and assign the property to the capable new owner.[76]

2.1.2 Distribution

In every social system, the distribution of income and wealth is considered as a prime factor to differentiate between one social system and another. The Islamic principle of income distribution is based on *al-A'dl* and therefore, negates the extremes of inequality. The concept of *al-'Adl* emphasizes equitability in the distribution of income and wealth as highlighted in al-Quran Surah *al-Hasyr* verse 59:7:

مَّآ أَفَآءَ ٱللَّهُ عَلَىٰ رَسُولِهِۦ مِنْ أَهْلِ ٱلْقُرَىٰ فَلِلَّهِ وَلِلرَّسُولِ وَلِذِى ٱلْقُرْبَىٰ وَٱلْيَتَٰمَىٰ
وَٱلْمَسَٰكِينِ وَٱبْنِ ٱلسَّبِيلِ كَىْ لَا يَكُونَ دُولَةًۢ بَيْنَ ٱلْأَغْنِيَآءِ مِنكُمْ
وَمَآ ءَاتَىٰكُمُ ٱلرَّسُولُ فَخُذُوهُ وَمَا نَهَىٰكُمْ عَنْهُ فَٱنتَهُوا۟ وَٱتَّقُوا۟ ٱللَّهَ
إِنَّ ٱللَّهَ شَدِيدُ ٱلْعِقَابِ ٧

(*al-Hasyr* 59:7)

Translation: What Allah has bestowed on His Messenger (Muhammad) from the town dwellers without having to fight, belongs to Allah, the Messenger, the kindred (of the Messenger), the orphans, the poor, and the wayfarers (who are stranded lacking provision and means of travel). (This decision is made) so that the wealth shall not be going round and round among those who are already rich among you. And whatever order which the Messenger (pbuh) brings to you, accept it and put it into practice, and whatever he forbids you from, you abstain from it and remain conscious of Allah. Allah is indeed stern in retribution (to those who set themselves against Him) [77]

The redistributive mechanism in Islam consists of feeding of the needy, giving of alms and the law of inheritance.

2.1.3 Economic Freedom

Economic freedom means to get involves in an economic activity freely without any coercion. Freedom is a cornerstone in Islam. Within the Islamic context, a sale and purchase transaction is considered void and null if the element of coercion exists. Thus, freewill is necessary in Islamic contracts. The prophet Muhammad S.A.W (Pbuh)

---

[76] *Ibid.*
[77] Department of Islamic Development Malaysia, *Tafsir ar-Rahman Interpretation of the Meaning of the Quran,* 1099.

adopted many measures as revealed to him (Pbuh) to ensure freedom in economic activities. This also includes the control measurement over unethical behavior in economy such hoarding, monopoly and manipulation of prices and alike.

2.1.4 Other Islamic Economic Values

2.1.4.1 Avoiding Israf

Israf or wasteful is among the worst behavior. Islam prohibits wasteful as evidenced in the Quran verses 17:27 and 7:31. The prohibition of wasteful is vital to ensure good consumerism and well utilization of goods and properties. Islam applies good consumerism in Muslim individual as practiced in their daily lives such as in using appropriate amount of water for ablution and in prohibiting wastefulness.

2.1.4.2 Consultative Governance

Islam applies the concept of *Shūra* in social organization. This concept is also known as consultative decision-making. This concept is evidenced in the Quran as stated in verse 3: 159. Furthermore, Allah guarantees His blessing on those who apply the *Shūra* concept in their affairs (42:38). Series of discussions among Islamic jurists and western scholars revealed that the concept of democracy would be exercised within an Islamic ethos and centers, around the concept of *Shūra*.[78] Table 2.1 demonstrates the main features of Islamic economics.

[78] M.A Muqtader Khan, "The Mythology of Islamic Economics and the Theology of the East Asian Economic Miracle," (Proceedings of the Fourth Harvard University Forum on Islamic Finance: Islamic Finance: The Task Ahead Cambridge, Massachusetts, Center for Middle Eastern Studies, Harvard University, 2011), 39.

Table 2.1: The Main Features of Islamic Economics

Guideline	Position of Islamic Economics
Legal Framework	- Law and the rule of law are important: linking government action to a superior law – *Sharī'ah* (which only contains some directly applicable economic content) and *Sharī'ah* – compliant secular law (the formulation of which gives a great creative leeway). - Concepts of an Islamic economic system are compatible with different forms of government (democracy, monarchy, etc.).
Property Ownership	- Legitimacy and protection of private property, even relating to the means of production, positive assessment of entrepreneurial achievement (Prophet as a role model). - One's own work/achievements should be the primary source of income and legitimate wealth; assets must be used productively (desired growth and employment effects).
Competition as a basis	- Justice is important: price fairness. Fair price: competitive price; state protection of competition against monopolization; occasional state intervention in the case of "sensitive" prices.
Application of the Principle of Liability	- Strong emphasis on opportunity and risk (particularly in the financial economy), skepticism towards limited liability legal structures, such as limited companies (now acceptable), increasing importance of corporate governance.
Stability of the Economic Environment	- Monetary stability is important: various models for stability – oriented monetary systems (gold standard, commodity currencies, one hundred percent money, monetary rules, etc). - Regulation of financial markets (*riba* ban, linking financial transactions to the real economy, prohibition of purely speculative trading).
Provision of public goods by the state	- Provision of a basis infrastructure (legal system, education, healthcare, mobility) recognized as a legitimate duty of the state; discussion about science as a public good. - Correction of market/competitive failure, no structural or procedural interventionism.
Solidarity and Social Security	- Poverty reduction as a primary economic objective. - Zakat at the core of a social security system that is independent of the family (claim of the needy in respect of society-state is subsidiary). - Calls for international solidarity within the Islamic world (*umma*). - Basic principle of insurance that conforms to *Sharī'ah* Law (*Takāful*) mutuality, entry into a shared risk community instead of purchasing risk coverage.
Incentive Compatibility	- Legitimacy of secular taxation (in addition to *zakat*) is now uncontroversial; exact structure can be defined according to time/place/circumstance, considering incentive compatibility.
Sustainability	- Allah is the ultimate owner, human beings are merely custodians, duty extends to future generations (idea of sustainability)
Open Markets	- In principle, for all open goods, services and labor markets, but reservations with capital markets (issue of interest,

	speculative capital transactions).

Source: Konrad-Adenauer-Stiftung: Guidelines for Prosperity, Social Justice and Sustainable Economy Activity, Berlin 2009.

2.2 PRINCIPLES OF ISLAMIC FINANCE

The operational system of Islamic finance is based on the Islamic law (*Sharī'ah*). This connotes the compulsory and obligation for human kind to comply with the *Sharī'ah* ruling during the application of Islamic finance. *In Sharī'ah,* there are some matters that are strictly prohibited to ensure the validity of business. This prohibition aims to secure fairness, just and accountability. The matters that *Sharī'ah* prohibits in business are *maysir* (gambling), *riba* (interest), *gharar* (uncertainty) and other activities, which may bring harm to the individual and social life. For example, doing business in gambling and liquor, charging interest on loans and selling robbery items.

2.2.1 Prohibition of Interest:

Riba is the most prohibited business dealing in the *Sharī'ah* law. The prohibition of *Riba* is evidenced in many chapters of the al-Quran such as Surah *al-Rum* (39), Surah *an-Nisaa'* (160-161), Surah *āli-Imran* (130) and Surah *al-Baqarah* (278-279). *Riba* is interpreted as "any unjustifiable increase of capital, whether in loans or sales." In normal banking and finance practices, *Riba* refers to any positive, fixed, predetermined rate tied to the maturity and the amount of principal (that is guaranteed regardless of the performance of the investment). Within the *Sharī'ah* law, banking and finance practices that have *Riba* features are prohibited.

Islamic scholars agree that *Riba* refers to a wide meaning. *Riba* does not only refer to usury, but also charging penalty on late payment against defaulters. The wisdom of this prohibition is to promote a well social life among mankind. Thus, Islam permits the earning of profit instead of *Riba* for the harmonization of human lives where this concept promotes entrepreneurship and creates additional wealth.

Therefore, charging interest in business in any situation may not create wealth but it creates barriers for successful businesses because the increment of the charges burdens the entrepreneur. Social justice could be portrayed as a situation where the borrowers and lenders share both rewards and losses in which this means a fair and just accumulation of wealth as a representative of true productivity.[79]

2.2.2 Money as "potential" capital:

In Islam, money is considered as a medium of transaction. People use money to buy and sell things. However, this understanding is different in the conventional finance where money is treated as "potential" capital. This means that money could become productive when it creates wealth through loans. In Islam, there is a concept of "time value of money." This concept applies when money is treated as capital and not "potential" capital.

2.2.3 Risk Sharing:

Due to the prohibition of interest, a supplier of funds becomes an investor rather than a creditor. In Islamic business joint venture, the provider of the financial capital and entrepreneur share business risks in return for a share of the profits. The term financial transaction needs to reflect a symmetrical risk-return distribution that each party in the transaction may face. Both investors and the financial intermediary share the profits and losses (if any), and the financial intermediary shares the risks with the investors.

Prohibition of speculative behavior: In order to promote just and certainty in business, the Islamic financial system prohibits any speculative behavior. This speculative behavior includes gambling (*Maysir*) and extreme uncertainty (*gharar fahish*) or risk. This understanding includes unethical business activities such as

[79] Hossein Askari, Zamir Iqbal, Noureddine Krichene, Abbas Mirakhor, *The Stability of Islamic Finance: Creating a Resilient Financial Environment for a Secure Future*, (Singapore: John Wiley and Sons (Asia) Pte. Ltd., 2010), 4-5.

hoarding and monopoly. Sanctity of contracts: Honest and disclosure are sacred behavior in Islam. In business practice, Islam upholds contractual obligations and the disclosure of information. These kinds of habits may reduce the risk of asymmetric information and moral hazard.

2.2.4 *Sharī'ah* -approved activities:

An essential difference between the Islamic financial system and the conventional counterpart is on the *Sharī'ah* compliant system. In contrast with the conventional system, the Islamic financial system is running under the Islamic law and guidelines. Only business activities, which do not violate the rules of *Sharī'ah* are permissible in business. For example, a business dealing involving alcohol, gambling or casinos is strictly prohibited.

2.2.5 Social justice:

Exploitation, injustice, hoarding and monopoly are examples for social injustice, which are strictly prohibited in Islam. Any financial transaction, which leads to the unjust behavior towards any parties are prohibited.

According to Abdul Mumin, the essence and the basic elements to form an Islamic financial system in terms of concepts and operations shall include the following matters:[80]

1. The activities involved in usury *riba* should be avoided and abolished completely in all dealings and transactions. Thus, all investment activities should be based on profit and loss sharing and there should be no opportunity for *riba* allowed in debt-based transactions.
2. All investment activities must be in accordance with principles and procedures outlined in the contract of *muamalah*. Among the principles of *Sharī'ah* is *Bay 'al-Murabahah, Al-Ijarah, ar-Rahn, Wakālah , Jua'lah,* and *Wadiah*.

---

[80] Ab. Mumin Ab. Ghani and Fadillah Mansor (eds), *Dinamisme Kewangan Islam Di Malaysia*, (Kuala Lumpur: University of Malaya Press, 2006), 4.

3. A business activity or project should be based on the participation in the production process rather than business debts. Hence, the banks and financial institutions must participate in production activities either as entrepreneurs or partners of the project.

In addition, the Islamic financial system should also take into account the main policy in forming the elements, namely:

i. It should be based on Islam entirely and not only in name and label, but it must also reflect the philosophy, values, ethics and objectives of the Islamic *Sharī'ah*.

ii. It should have the features of a viable and sophisticated system and be able to compete with the conventional systems in all aspects. To realize this purpose, three prerequisites must be contained in an Islamic financial system:

   a. Having a variety of instruments. Various instruments must be created to meet the needs of different communities. If the Islamic financial instruments are not diversified, then there is a problem of idle funds due to the lack of investment opportunities and financing tools.

   b. Having many and sufficient institutions to support demand. Having sufficient institutions is vital because it contributes an in-depth and enhances the system. Other than that, a huge number of institutions in the financial system would provide competitive market in which each institution would strive to be better by enhancing the quality in their services and products in order to attract customers. This, will indirectly improve the service and the quality of products.

   c. Creating a market mechanism. To create a market mechanism that links the institutions and instruments. The Islamic financial system should create a mechanism on how to link institutions and instruments to ensure that there is an efficient market channels for the system to do business. For instance, the creation of the money market system between Islamic banks and the creation of mechanism for the Islamic capital market.

2.3 ISLAMIC FINANCE REGULATORS IN MALAYSIA

2.3.1 Central Bank of Malaysia

The central bank of Malaysia or known as Central Bank of Malaysia was established in 1959. Central Bank of Malaysia is governed under the Central Bank of Malaysia Act 1958 (revised 2009). Section 3(1) states that notwithstanding the repeal of the Central Bank of Malaysia Act 1958 by section 99, the body corporate established under the repealed Act under the name "Bank Negara Malaysia" or, in English, "Central Bank of Malaysia" shall continue to be in existence under and subject to the provisions of this Act. The Act incorporates an explicit mandate, provides comprehensive provisions for heightened surveillance, pre-emptive actions and expanded resolution powers to facilitate the swift and orderly resolution of a financial crisis. The bank[81] may also take appropriate intervention to avert risks that stem from unregulated entities. Everything that is related to Islamic finance is discussed in thorough in part VII of the Act. Section 5(1) lays down the principal objects of the Bank to promote monetary stability and financial stability conducive to the sustainable growth of the Malaysian economy. As written in section 5(2) the primary functions of the Bank are as follows:[82]

a. To formulate and conduct monetary policy in Malaysia;
b. To issue currency in Malaysia;
c. To regulate and supervise financial institutions which are subject to the laws enforced by the Bank;

[81] Section 2(1) of the Central Bank of Malaysia Act define "Bank" means Bank Negara Malaysia" or in English, the "Central Bank of Malaysia."
[82] Law of Malaysia, Act 701, Central Bank Act 2009, 15.

d. To provide oversight over money and foreign exchange markets;

e. To exercise oversight over payment systems;

f. To promote a sound, progressive and inclusive financial system;

g. To hold and manage the foreign reserves of Malaysia;

h. To promote an exchange rate regime consistent with the fundamentals of the economy; and

(1) To act as the financial adviser, banker and financial agent of the Government.

(2) The Bank shall have all the powers necessary, incidental or ancillary to give effect to its objects and carry out its functions.

(3) The Bank in giving effect to its objects and carrying out its functions under this Act shall have regard to the national interest.

2.3.2 Securities Commission

Malaysia's Security Commission was set up in 1993 and governed under the Securities Act 1993. The SC is organized under the Ministry of Finance and therefore, it directly reports to the Minister. The SC is attached to investigate and enforce power and is a self-funded statutory body. The role of SC is stated in Section 15 of the Securities Commission Act 1993 as follows: [83]

a. To advise the Minister on all matters relating to securities and futures industries;

b. To regulate all matters relating to securities and futures contracts;

c. To ensure that the provisions of the securities laws are complied with;

d. To regulate the take-over and mergers of companies;

e. To regulate all matters relating to unit trust schemes;

f. To be responsible for supervising and monitoring the activities of any exchange holding company, exchange, clearing house and central depository;

[83] Securities Commission Act 1993 (ACT 498), 13-15.

g. To take all reasonable measures to maintain the confidence of investors in the securities and futures markets by ensuring adequate protection for such investors;

h. To promote and encourage proper conduct amongst participating organizations, participants, affiliates, depository participants and all licensed or registered persons of an exchange, clearing house and central depository, as the case may be;

i. To suppress illegal, dishonorable, and improper practices in dealings in securities and trading in futures contracts, and the provision of investment advice or other services related to securities or futures contracts;

j. To consider and make recommendations for the reform of the law related to securities and futures contracts;

k. To encourage and promote the development of securities and futures markets in Malaysia including research and training in connection thereto;

l. To encourage and promote self-regulation by professional associations or market bodies in the securities and futures industries;

m. To license and supervise all licensed persons under any securities law;

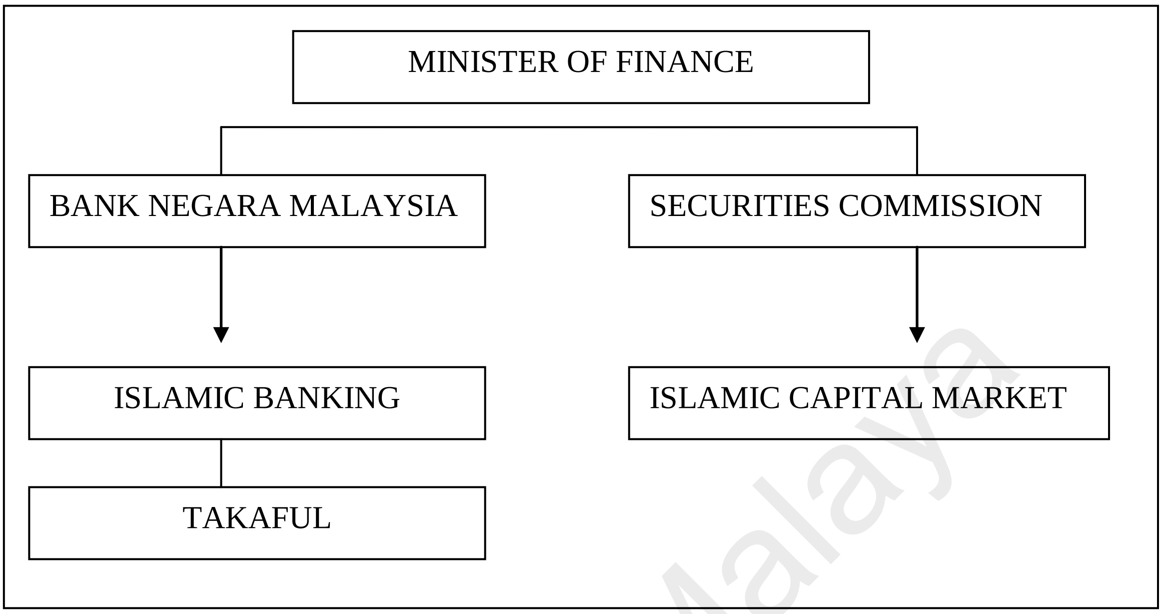
n. To promote and maintain the integrity of all licensed persons in the securities and futures industries.

(3) The Commission shall have the functions and powers conferred upon it by or under the securities laws;

(4) Nothing in paragraph (1)(1) shall limit or otherwise affect the functions of the Commission.

(5) For the purposes of this section, “depository participants” means persons to whom section 9 of the Securities Industry (Central Depositories) Act 1991 applies.

Diagram 2.1: The following diagram shows the governance system of both Central Bank of Malaysia and the Securities Commission of Malaysia:



2.4 ISLAMIC FINANCE INSTRUMENTS

The vital role of Islamic financial institutions is to fully adopt the *Sharī'ah* principles in their business activities such financial contracts, effective resource allocation, investment in development projects, profitable placement of surplus funds, *Sharī'ah* -compliant products/services, etc. All the above functions have *Sharī'ah* justifications and principles. There are a number of *Sharī'ah* compliant contracts approved by Muslim jurists in order to facilitate Islamic banks in delivering their products and services. Basically, these contracts can be broadly classified into the following categories:

2.4.1 Exchange-based contract ('*Uqud al-Mua'wadhāt*)

Exchange-based contracts are contracts whereby two transacting parties entered into a contract to acquire ownership of an asset or commodity, which ends up with the transfer of ownership of the exchanged counter-values. The exchanged counter-values can either be in situations where the gain of usufruct in a lease contract or a corporeal thing in a currency exchange, forward sale and manufacturing contract. These contracts are founded upon the principle of justice in the sense that the rights of both parties are to be fulfilled at a minimum or obligatory level.[84]

There are two main categories included under the exchange-based contracts, namely sale-based contracts and lease-based contracts. Both categories comprise of the following examples of contracts:

2.4.1.1 Sale-based contracts:

a. *Al-Murābahah*
b. *Bay' al-Salam*
c. *Bay' al-Istisna'*
d. *Bay' al-Dayn*
e. *Bay' al-Sarf*
f. *Bay' al-Tawarruq*
g. *Bay' al-I'nah*

2.4.1.2 Lease-based contract:

a. *Al-Ijarah*

2.4.2 Charity-Based Contract (*'Uqud al-Tabarru'at*)

Charity-based contracts are contracts based on benevolence (*Ihsan*) and co-operation (*Ta'awun*), which does not require the exchange of something for another thing. Therefore, an asset ownership in this regard is acquired without any counter-value. The examples of charity-based contracts are as follows:

[84] International Sharīʾah Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations*, 201.

a. *Qard* (Benevolent Loan)

b. *Hibah* (Gift)

c. *Sadaqah* (charity)

d. *Waqf* (endowment)

e. *I'arah* (asset borrowing)

In a certain situation, any attempt to impose additional cost on a benevolent loan is a violation of the very purpose of the charity-based contract. Thus, such increment on the principle loan is prohibited and in contrast of the principle of *tabarru'* such as *ihsan* and *ta'awun.*

2.4.3 Waiving Contracts (*'Uqud al-Isqātāt*)

Waiving contracts are contracts which are entered into by someone to waive a right that has been established in one's liability whether with or without a counter-value. If it is affected without a counter-value such as a rebate (*Ibra'*) and the right of pre-emption (*shuf'ah*) is waived, then it is called *isqath mahd* (purely waiving contract) and if otherwise, then it is termed as *isqath al-mua'wadhah.*

2.4.4 Partnership Contracts (*'Uqud al-Isytirak*)

Partnership contracts refer to contracts, which are entered into for the purpose of work and profit. It is founded upon the spirit of co-operation and partnership in the sense that profits are shared together by the partners and losses are borne by both of them (in a partnership contract and all of its type), and borne by the capital provider *(rabbul mal*) in a *mudhārabah* contract. Other examples of partnership-based contracts are the *muzāra'ah* and *musāqah,* which also have the elements of co-operation and risk-sharing.

2.5 *SHARĪ'AH* FRAMEWORK IN ISLAMIC FINANCE

Sharī'ah literally means, "the road to the watering place" or the straight path to be followed." The Quran has used the word *Sharī'ah* with this meaning in the following verse:

ثُمَّ جَعَلْنَٰكَ عَلَىٰ شَرِيعَةٍ مِّنَ ٱلْأَمْرِ فَٱتَّبِعْهَا وَلَا تَتَّبِعْ أَهْوَآءَ
ٱلَّذِينَ لَا يَعْلَمُونَ ١٨

(*Al-Jāthiyah* 45:18)

> Translation: And now, We have set you (O Muhammad, and sent you) to help establish a way of religion (complete) constituting rules of religion; so you follow that way and do not yield to the desires of those who are ignorant (of the truth). [85]

Basically, the structure of *Sharī'ah* is upheld by three main pillars, namely al-*Ahkam al-I'tiqadiyyah* (matters related to beliefs), *al-Ahkam al-Akhlaqiyyah* (matters related to moral and ethics) and *al-Ahkam al-A'māliyyah* (matters related to the relationship between individual and others which also known as *Fiqh*).

The use of the term "*Sharī'ah*" in Islamic finance, basically refers to the compliant aspect of Islamic financial products and services. In the current practice, in Islamic finance products and services, the word "*Sharī'ah*" is used to refer to the "*Sharī'ah*"-compliant and "*Sharī'ah*"-based.[86]

2.5.1 *SHARĪ'AH* SUPERVISORY SYSTEM

[85] Department of Islamic Development Malaysia, *Tafsir ar-Rahman Interpretation of the Meaning of the Quran,* 979.
[86] *Ibid.,* 148.

The *Sharī'ah* Supervisory board is among the main factors that strengthen the Islamic finance structure. This *Sharī'ah* body is known in various names such *Sharī'ah* Committee, *Sharī'ah* Advisory Council and *Sharī'ah* Supervisory Board. The prime role of the *Sharī'ah* board is to monitor the Islamic Finance Institution's (IFI) operations and provide *Sharī'ah* resolution on related issues through collective *Ijtihad*. Among the roles of the *Sharī'ah* board is to function as a control mechanism in supervising the matters related to *Sharī'ah* compliance in which this includes the payment of Zakat. In depth elaboration, the objective of *Sharī'ah* board is to consult IFI's in the matter related to the setting up of policies and regulations based on *Sharī'ah*, to ensure all financial transactions are approved in *Sharī'ah* from the legal aspect and compliance side and also to prepare their future contracts based on the Islamic law.

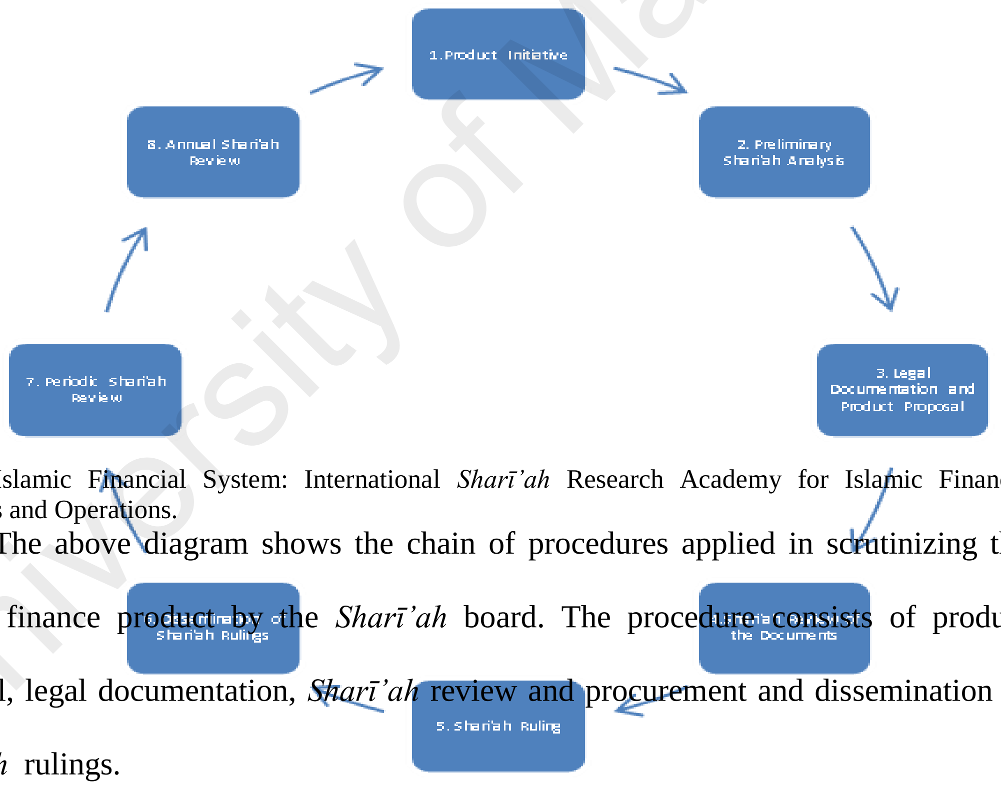
In Malaysia, the term "*Sharī'ah* Supervisory" is used in various names that reflect different bodies. The term "*Sharī'ah* Advisory Council," is used in referring to the *Sharī'ah* Supervisory Board in the Central Bank and the Securities Commission. On the other hand, the term "*Sharī'ah* Committee" is used to refer to the *Sharī'ah* supervisory bodies in Islamic finance institutions. Although various terms are used in referring to the *Sharī'ah* advisory bodies, they share common objectives and responsibilities.

The Central Bank of Malaysia guideline, number IV (7) clearly states that every IFI is required to appoint a *Sharī'ah* committee member. The statement says: Every Islamic financial institution is required to establish a *Sharī'ah* Committee. In the situation where Islamic finance institutions have two sectors of Islamic banking and

Takāful, the *Takāful* segment must establish its own *Sharī'ah* Committee, due to the legal requirement under Takāful Act.[87]

The members of SAC of Central Bank of Malaysia are conferred by His Majesty of Malaysia and, hence, becoming the highest *Sharī'ah* Authority in Islamic finance. Under the SAC purview, all matters related to Islamic finance in Malaysia are under the supervision of the SAC. This includes the ascertainment of the Islamic law for Islamic banking and *Takāful* business or any other business, which is under the *Sharī'ah* principles and is supervised and regulated by Central Bank of Malaysia.[88]

Diagram 2.2: The functions of the *Sharī'ah* Board are presented in the following diagram:



Source: Islamic Financial System: International *Sharī'ah* Research Academy for Islamic Finance, Principles and Operations.

The above diagram shows the chain of procedures applied in scrutinizing the Islamic finance product by the *Sharī'ah* board. The procedure consists of product proposal, legal documentation, *Sharī'ah* review and procurement and dissemination of *Sharī'ah* rulings.

---

[87] Bank Negara Malaysia, "BNM Guidelines," Bank Negara Malaysia Website, retrieved on 29 May 2013,
http://www.bnm.gov.my /guidelines/03_dfi/03_prudential/03_gl_governance_of_Sharī'ah _committee.pdf.

[88] Bank Negara Malaysia website, "Learn About the Bank," retrieved on 7 Jun 2013, http://www.bnm.gov.my/index.php?ch=7&pg=715&ac=802.

The *Sharī'ah* board's functions could be divided into three major tasks: the issuance of *fatwa* via collective (*ijtihād*), review (*mutābaah*) and supervision (*raqābah*).[89]

2.6 THE STRUCTURE OF THE ISLAMIC FINANCIAL SYSTEM IN MALAYSIA

In principle, the Islamic financial system shares the same structure with its conventional counterparts. However, there is one main factor that differentiates each other which is the "*Sharī'ah* factor." This factor acts like a filter mechanism to make a faulty status for any product breaches the *Sharī'ah* requirement.

The government of Malaysia is keen on developing the country as an Islamic finance country and to make the presence of the Islamic financial system parallel with the conventional financial system. This development effort involves not only the Islamic banking system, but also the entire Islamic financial system such as *Takāful* and Islamic financial market.[90]

The task of developing a successful Islamic financial system is indeed not an easy one. It requires the formulation of a sound plan and well-coordinated efforts from various parties. Now, Malaysia has successfully developed an integrated Islamic financial system comprising the following categories:

1. Islamic Banking System
2. Islamic Insurance or Takāful
3. Islamic Financial Market which consist of two segments:

   3.1 Islamic Capital Market

   3.2 Islamic Money Market

[89] International Shari'ah Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations*, 709.

[90] Sudin Haron, "Towards Developing a Successful Islamic Financial System: A Lesson from Malaysia," (Working Paper Series 003, 2004), 2.

Currently, Malaysia is regarded as the most advanced in the Islamic banking system with a progressive and robust system compared to other Muslim countries. This is evidenced from the implementation of the Islamic banking system in Indonesia and Brunei in which they use the Malaysian model in the earlier period of the establishment of the Islamic banking system in their respective countries.[91]

2.6.1 ISLAMIC BANKING SYSTEM

Basically, there are similar structure and framework of the Islamic banking system and the conventional financial system counterpart. Some may assume that there are almost no differences between both financial systems. However, in the true sense, an Islamic banking system operates under the supervision of *Sharī'ah*, which makes the Islamic banking system has a major difference with the conventional counterpart. Further, the Islamic banking system functions based on the principle of mutual risk and profit sharing between parties. The financing system in the Islamic banking is based on the sale and purchase of the underlying assets, in which this may secure the interest of both parties. This framework is also backed by the Islamic banking's core values whereby activities that promote entrepreneurship, trade and commerce that bring societal development or benefits are encouraged. Any activity that mixes up interest (*riba*), gambling (*maisir*) and speculative trading (*gharar*) is strictly prohibited.

Al-Jarhi and Iqbal defined an Islamic bank as follows:[92]

"The function of an Islamic bank is to restore deposit and execute banking activities such as borrowing and lending which do not involve the charging of interest.

---

[91] *Ibid.*

[92] Al-Jarhi, M and Iqbal M, "Islamic Banking: Answers to Some Frequently Asked Questions," (Occasional Paper No.4, Islamic Research and Training Institute, Islamic Development Bank, Jeddah, 2001), 23.

In terms of liabilities segment, an Islamic bank implements a *mudhārabah* contract. Simultaneously, the service also includes the acceptance of demand deposits based on free-interest loans from the clients to the bank and it is backed with a guarantee."

In term of assets segment, it facilitates funds based on profit and loss sharing or based on a debt creation, which complies with *Sharī'ah*. Further, it functions as the manager of investment on behalf of the owner during time deposits, normally known as investment deposits.

Among others, equity holdings and trading of asset and commodity formed a vital structure of the Islamic banking system. Shares of an Islamic bank are divided among the depositors based on the size and date to maturity of each deposit. Sufficient information must be delivered to the depositors regarding the ratio of shares on bank's net earnings.

In the history of the establishment of Islamic banking, many writings have referred to the *Mit Ghamr* Local Savings Bank, established in Egypt in 1963 as the first Islamic bank. In Malaysia, Muslim Pilgrim's Savings Corporation was first established in 1963. This institution is the first Islamic financial institution in Malaysia. Its paramount objective is to help people to commit their saving on a regular basis for their pilgrimage to Mecca. Later in 1969, it evolved into the Pilgrim's Management and Fund Board or known as Lembaga Tabung Haji.[93] However, Lembaga Tabung Haji cannot be considered as a bank but more towards a social service in assisting the Muslim community to perform pilgrimage and it was later expanded to involve in investment and economic activities in order to generate profit from depositors fund.

The path towards the establishment of Islamic banking in Malaysia started on 30th July 1981 when the government appointed a National Steering Committee of Islamic Bank. After a year, the committee proposed a conceptual framework for the

---

[93] International Shari'ah Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations*, 298.

licensing and supervising of the Islamic banking system in Malaysia.[94] Finally, the government approved the Islamic Bank Act 1983 (IBA), which was effective on 7 April 1983. This was substituted by the announcement of the first Islamic bank, the Bank Islam Malaysia Berhad (BIMB) in July 1983. This effort is a mirror of the revival of interest and the increasing demand from Malaysian Muslims for the *Sharī'ah* -based banking and financial services.[95]

BIMB has played a vital role in the development of Islamic banking system in Malaysia and its presence in Malaysia has reached to almost 30 years. BIMB has successfully expanded their business throughout the country and simultaneously contributed to the development of new products in the financial market. Under the structured plan of the Islamic banking strategy, Malaysia enjoys a well-coordinated and systematic Islamic banking development. The development of the Islamic banking system in Malaysia can be divided into three phases.

The first period between the years 1983 until 1992 is considered as the period of familiarization for Islamic bank. Within this period, the IBA act was officially passed and enacted and subsequently, the first Islamic bank, BIMB was established. The second period is between the years 1993 until 2003 where the landscape of Islamic banking system in Malaysia was adorned by the competition among banks. More development and expansion initiatives resulted in the permission for conventional banks to offer Islamic banking services through the Islamic counter named as Islamic window in 1993. Further, the third stage began from the year 2004 and it is considered as the period of financial liberalization. The CBM has intensified efforts to develop Malaysia as an International Islamic banking country by liberalizing domestic market, which resulted in the opening of new foreign Islamic banks in Malaysia. Within this period,

---

[94] Zamri Bin Hassan, "Islamic Banking: Its legal Impediments and Reformation with Special Reference to Malaysia," *Law Majalla*, Vol. 1, (2002), 97.

[95] International *Shari'ah* Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations,* 298.

permission had been given to conventional banks to open their full-fledged Islamic banks via their subsidiaries.[96]

2.6.1.1 ISLAMIC BANKING INSTRUMENTS

The Islamic banks function like the conventional banks where both banks become as mediums to channel savings fund to the customers for the purpose of consumption and capitalization. The implementation of *riba* is clearly restricted in Islam and thus, the Islamic banks must provide a free *riba* financing to the customers. Hence, the products and services in Islamic banks must comply with *Sharī'ah* . For this purpose, all products must be under *Sharī'ah* screening process, in which the *Sharī'ah* officer will evaluate the products based on the authentic and fundamental Islamic law of Quran and Hadith prior to offering the products to the customers.[97]

The principle of Islamic banking instruments based on *Sharī'ah* comprises five major categories as follows: [98]

1. Profit and loss sharing principles.
2. Sale and purchase principle.
3. Principles on which fees and charges are based.
4. Free services principles.
5. Ancillary principles.

In term of product development in Malaysia, there are many Islamic financial products that have been introduced along the years since the commencement of Islamic bank in Malaysia in 1983. It could be described that Malaysia has successfully

[96] Hamim S. Ahmad Mokhtar, Naziruddin Abdullah & Syed M. Alhabshi, *Efficiency and Competition of Islamic Banking in Malaysia,* (United Kingdom: Emerald Grouping Publishing Limited, Vol. 24 No.1, 2008), 31.
[97] Sudin Haron, Wan Nursofiza Wan Azni, *Islamic Finance and Banking System: Philosophies, Principles and Practices*, (Selangor, Malaysia: McGraw-Hill (Malaysia) Sdn. Bhd., 2009), 128.
[98] *Ibid.*, 129.

developed a well and comprehensive Islamic financial products and instruments to be at par with the conventional counterpart. Islamic financial products features are totally different than the conventional financial products in which the Islamic financial products must be free from *riba* elements and able to adapt the characteristics of conventional instruments. Among other features are;[99] it can be traded, the ability to easily transferable from one owner to another owner, it must be "liquid" (that is easy to sell when requiring cash), it should lead to minimal risk and it must be simple and easy on pricing.

Table 2.2: The following table shows the range of Islamic banking products and services applied in Malaysia:

Product Category	**Concept Used**
A. Deposit	
1. Current Account-i	Wadiah Yad Dhamānah/ Murābahah/ Qard
2. Savings Account-i	Wadiah Yad Dhamānah/ Mudhārabah/ Qard
B. Other Deposit	
1. Commodity Murabahah	Murābahah/ Tawarruq
C. Investment	
1. General Investment Account-i	Mudhārabah/ Qard
2. Special Investment Account-i	Mudhārabah
3. Specific Investment Account-i	Mudhārabah
D. Financing (Fund – Based)	
1. Asset Financing-i	Tawarruq/ Murābahah/ Mudhārabah/ Musyārakah/ Ijārah
2. Asset Based Financing-i	Ijārah
3. Benevolent Loan-i	Qard
4. Block Discounting-i	Bay' Dayn
5. Bridging Finance-i	Istisna'/ Bai' Bithaman Ajil
6. Bungalow Lots Financing-I	Bai' Bithaman Ajil
7. Cash Line Facility-i	Bai' I'nah/ Bai' Bithaman Ajil / Murabahah
8. Club Membership Financing-I	Bai' Bithaman Ajil
9. Commodity Murabahah Financing-I	Murābahah/ Tawarruq
10.Computer Financing-I	Bai' Bithaman Ajil
11. Contract Financing-I	Bai' Bithaman Ajil/Murābahah/Istisna'
	Musyārakah/Mudhārabah/Ijarah
12. Education Financing-I	Murabāhah/ Bai' Bithaman Ajil/ Bai' I'nah
13. Equipment Financing-I	Bai' Bithaman Ajil
14. Factoring Facility-I	Bai' Dayn
15. Fixed Asset financing-i	Bai' Bithaman Ajil
16. Floor Stocking Financing-i	Murabahah/ Bai' Bithaman Ajil
17. Hire Purchase Agency-i	Wakālah

[99] Abd. Mumin Ab. Ghani and Fadillah Mansor, *Dinamisme Kewangan Islam Di Malaysia*, 6.

18. Home/House Financing-i	Bai' Bithaman Ajil/ Istisna'/ Variable Rate Bai' Bithaman Ajil
19. Industrial Hire Purchasei-i	Ijarah
20. Land Financing-I	Bai' Bithaman Ajil
21. Leasing-I	Ijārah
22. Pawn broking-I	Rahnu (Qard and Wadiah Yad Dhamāanah) / Rahnu (Qard)
23. Plant and Machinery Financing-I	Bai' Bithaman Ajil/ Istisna'/ Ijarah/
24. Project Financing-I	Bai' Bithaman Ajil/ Istisna'/ Ijarah/ Musyarakah/ Mudhārabah / Tawarruq/ Murābahah
25. Property Financing-I	Bai' Bithaman Ajil/ Istisna'/ Variable Rate Bai' Bithaman Ajil
26. Revolving Credit Facility-i	Bai' Bithaman Ajil/ Murābahah/ Hiwālah/ Bai' I'nah
27. Share Financing-i	Bai' Bithaman Ajil/ Bai' Inah
28. Shop House Financing-i	Bai' Bithaman Ajil/Istisna'/ Variable Rate Bai' Bithaman Ajil.
29. Sundry Financing-i	Bai' Bithaman Ajil
30. Syndicated Financing-i	Istisna'/ Bai' Bithaman Ajil/ Ijārah
31. Term Financing-i	Bai' Bithaman Ajil/ Variable Rate Bai' Bithaman Ajil
32.Tour Financing-i	Bai' Bithaman Ajil
33. Umrah & visitation Financing-i	Bai' Bithaman Ajil
34. Vehicle/ Automobile Financing-i	Ijarah/ Bai' Bithaman Ajil/ Murabahah
35. Working Capital Financing-i	Murābahah/ Bai' Bithaman Ajil/ Tawarruq/ Murābahah/ Musyārakah/ Mudhārabah
E. Financing (Fee-Based)	
1. Accepted Bills-i	Murābahah/ Bai' Dayn
2. Bank Guarantee	Kafālah
3. Bills of Exchange-i	Wakālah
4. Export Credit Refinancing	Murābahah/ Bai' Dayn
5. Letter of Credit-i	Wakālah/ Murābahah/ Ijārah/ Bai' Bithaman Ajil
6. Shipping Guarantee-i	Kafālah
7. Trust Receipt-i	Wakālah/ Murābahah
F. Trade Finance	
1. Accepted Bills-i	Murābahah/ Bai' Dayn
2. Bank Guarantee-i	Kafālah
3. Bills of Exchange-i	Wakālah
4. Export credit Refinancing-i	Muarābahah/ Bai' Dayn
5. Letter of Credit-i	Wakālah/ Murābahah/ Ijārah/ Bai' Bithaman Ajil
6. Shipping Guarantee-i	Kafālah
7. Trust Receipt-i	Wakālah/ Murābahah
G. Card Services	
1. Charge Card-i	Qard
2. Credit Card-i	Bai' I'nah/ Bai' Bithaman Ajil
3. Debit Card-i	Ujr

Source: Malaysia International Finance Centre (MIFC) Official Website: (http://www.mifc.com/index.php? ch=38&pg=104&ac=28&bb=268).

2.6.1.1.1 *Sharī'ah* Compliant and *Sharī'ah* Based Product

There are two fundamental methods being used in developing the Islamic finance products, namely *Sharī'ah* -compliant instrument and *Sharī'ah* -based instrument. *Sharī'ah* - based instruments are contracts that originally exist and practiced among Muslims for a long time. On the other hand, generally, *Sharī'ah* compliant instrument is a modified conventional product to meet and comply with *Sharī'ah* requirements and later rebranded into an Islamic brand. Specifically, *Sharī'ah* compliance means adherence and conformity with the *Sharī'ah* principles. In the context of Islamic financial transactions, this means that all the financial transactions must comply and conform to Islamic law and rules of commercial transactions (*ahkam fiqh al mua'malat*). Hence, *Sharī'ah* compliant products may have its origins in conventional banking. To make a financial instrument *Sharī'ah* compliant, all that needs to be done is to remove those elements or components which contradict with *Sharī'ah* and replace them with a *Sharī'ah* acceptable concept. Multiple contracts may be used to facilitate and complete the transaction and inevitably some form of legal trickery could be involved. For instance, the product of *al-Ijarah Muntahia Bit Tamleek* (AITAB) is a contract derived from the hire and purchase conventional product, but by going through the *Sharī'ah* screening process, the product has presently become a *Sharī'ah* -compliant product, which uses the *Ijarah* (Hire) and Bay' (Sale) contracts. Thus AITAB product is a structured product from the original conventional product transformed into the *Sharī'ah*-compliant product based on the *Ijarah* (Hire) and *Bay'* (sale) contract.

Bai' Bithaman Ajil (BBA) product is another example for *Sharī'ah*-compliant product. BBA is a contract of deferred payment sale i.e. the sale of goods on deferred payment basis at an agreed selling price, which includes a profit margin agreed by both parties. Profits in this context is justified since it is derived from the buying and selling transaction as opposed to interests accruing from the principal lent out. In Malaysia, BBA is applied in facilitating the house financing. All the components to determine the selling price has to be fixed because the selling price has to be fixed at the time the contract is made, Hence, the profit rate for BBA financing is fixed throughout the period of financing. Unlike original *Murābahah*, BBA is developed to facilitate credit purchase and the deferred price is a marked up price, which is higher than the normal cash basis.

This is done due to the delayed payment reflected in the time value of money. Hence, the BBA product is especially modified to fulfill the financing facility in Islamic banks and financial markets.

A *Sharī'ah* based product is a financial instrument which is derived from the laws of *Sharī'ah*. It may share some similarities with existing conventional products but it did not originate form any conventional products. Structuring *Sharī'ah* based financial solutions is easier because there is no need to find ways to circumvent *Sharī'ah* prohibitions in order to achieve *Sharī'ah* compliance. The *Sharī'ah*-based products are such as *Murābahah, Bay' I'nah, Ijarah, Ujr, Salam,* and *Istina.'* The use of these products for a long period of time is approved by the Islamic scholars and unlike the *Sharī'ah*-compliant product, there is no amendment and modification on the original structure of these products. Hence, the products are originally *Sharī'ah*-based.

2.6.1.1.2 Islamic Finance Product Harmonization

The issue pertaining to the Islamic finance products is narrowed to the different views among Islamic scholars on certain Islamic contracts. For instance, a product based on *Bai' I'nah* is permissible in Malaysia but not in the Middle East countries. Thus, the differences in opinions and rulings need a mechanism of harmonization to ensure that there is no conflict among Islamic finance contracts around the world. Currently, the Islamic finance scholars opted to respect others' opinions as a normal practice when the opinions are different among them. This nature of respect could promote more *Sharī'ah* views, which assist in developing various Islamic finance products. The consideration in selecting juristic opinion must be based on the acceptance and marketability of the Islamic financial products.

As such, a product will remain available and could sustain in the market if there is a good demand from the customers. Hence, it is the customers who will decide whether the product will be successful or not. Therefore, prior to the marketing of certain products, the evaluation on the product acceptance must be taken into a high consideration by the product development team.

In order to harmonize differences among scholars, a strategic effort should be taken by developing an internationally accepted product. A person involves in a product development team must take this point clearly. The regulators and authorities must also play a vital role in promoting this effort by giving incentives and lifting up the barriers.[100]

2.6.1.2 ISLAMIC BANKING REGULATIONS IN MALAYSIA

To facilitate the Islamic banks to meet the objectives of a Central Bank, it should be empowered with comprehensive legal powers under the following legislation to regulate and supervise the financial system. These legislations include:

Table 2.3: Islamic Banking Regulations in Malaysia

1.	Islamic Financial Services Act 2013
2.	Banking and Financial Institutions Act 1989 (BAFIA)
3.	Islamic Banking Act 1983
4.	Development Financial Act 2002 (DFIA)
5.	Central Bank of Malaysia Act 1958 (CBMA)

2.6.1.2.1 Islamic Financial Services Act 2013

In order to strengthen the Islamic banking and finance legislation, the Central Bank of Malaysia has introduced a new law to replace the IBA act and BAFIA act. This new law named as Islamic Financial Services Act 2013 (IFSA), which among other aims to develop a robust effective risk governance to avoid uncertainty risks for the security of financial institutions. Putting this new act in effect will give a greater impact to many sectors of Islamic banking regulation such as audit compliance, insurers, talent

[100] Muhamad Muda, Abdullah Jalil, "Islamic Financial Product Development: Sharīʼah Analysis," (IIUM International Conference on Islamic Banking and Finance (IICiBF), Malaysia, 2007), 13.

recruitment, individual shareholding and company restructuring. Despite the banking sector, the act will also impact the *Takāful* industries.

Malaysia's new Islamic Financial Services Act (IFSA) has been introduced to provide a stronger legal foundation to spur the growth of Islamic finance sector. The Act provides a legal platform for development of Islamic finance in Malaysia which is reflected upon a comprehensive regulatory framework on specificities of the various Islamic financial contracts and supports on the effective application of Shariah financial contracts in the offering of Islamic financial products and services.[101]

This marked a significant milestone in aligning the shariah requirements of Islamic financial services in regulatory principles.[102]

Table 2.4: Contract Based Regulatory Framework

Islamic Finance: **Islamic Banks conduct financial intermediation functions using Shariah contracts**			
Shariah Standards Compliance with fundamental requirements of respective Shariah contracts	**Operational Standards** Strengthened risk management, governance, transparency and disclosure, market conduct and other operational aspects of applying Shariah standards.	**Shariah Standards** Codification of the role of the Shariah committee and board of directors of financial institutions in ensuring Shariah compliance	**Resolution** Priority of Payment reflective of underlying Shariah contractsa

gn the regulatory princ ah r

s e (3) noteworthy featur new

Table 2.5: Islamic Finance Contract

Asset	**Liabilities**

[101] International Center for Education in Islamic Finance (IFSA), Islamic Financial Services Act (FSA) and
Financial Services Act (FSA) , INCEIF Website, retrieved on 6 April 2016, http://www.inceif.org/islamic-finance/islamic-financial-services-act-2013/

[102] *Ibid.*

Sales Based	Equity Based	Fee Based	Islamic Deposits	Investments *Accounts (Equity)*	Investment Accounts (Other)
• *Murabahah* • *Istisna'* • *Ijarah* • *Tawarruq*	• *Mudharabah* • *Musharakah*	• *Wakalah* • *Kafalah*	• *Wadi'ah* • *Qard* • *Tawarruq*	• *Mudharabah* • *Musharakah*	• *Wakalah*

In effort to align the regulatory principles with the Shariah requirements in the services, there are three (3) noteworthy features embedded in the new legislation.

Table 2.6: IFSA Features

Define clearly the scope of asset and liabilities in Islamic Banking	**Provision governing takaful business clearly account for the nature of Shariah contracts in**	**Provide legal framework for the resolution of Islamic financial institutions in line with elements of relevant Islamic contracts**
Liability: The use of principal-guaranteed Shariah contracts such as qard, wadi'ah and tawarruq in deposit-taking is clearly distinguished from principal non-guaranteed Shariah contracts for investment such as mudarabah and wakalah Asset: The scope of financing activities similarly draws on the distinctive features of Islamic contracts to include equity and partnership financing contracts such as musharakah mutanaqisah, lease-based financing contracts such as Ijarah muntahia bittamleek, and fee-based	The Act gives legal effect to separation on fund between takaful operators sharholders and takaful participants. The regulatory requirements emphasise the fiduciary relationship between Takaful operators and takaful participants as stipulated in mudarabah or wakalah contracts requiring takaful funds to be managed on behalf and in the best interests of the takaful participants	Asset managed by Islamic bank are legally restricted from assets of the bank to prohibit any co-mingling of funds. Similarly applied to Islamic windows; Islamic asset and funds are separated from its conventional business In the event of the resolution of an Islamic financial institution, payments to Islamic depositors are prioritized in as stipulated in the guaranteed nature of contracts employed in Islamic deposit Similarly for Takaful funds and shareholder funds are separated and utilized to meet the respective liabilities in the event of a winding-up of a Takaful operator. These obligations differ in priority based on the specific contracts underlying the takaful business mode.

...nsi

place, it is with hope that the

Malaysia will further spur and that this move may be taken as an example for other key markets in advancing the islamic financial system together at global scale.[103]

2.6.1.2.2 Islamic Banking Act 1983

The Islamic Banking Act 1983 was approved by the parliament of Malaysia prior to the setting up of Bank Islam Malaysia Berhad. This law applies to all Islamic

---

[103] *Ibid.*

banking institutions operating in Malaysia. The Law consists of eight parts as follows:[104]

1. Short title, commencement, application and interpretation.
2. Provisions related to licensing.
3. Financial requirements and duties.
4. Matters related to ownership, control and management.
5. Restrictions on business.
6. Powers of supervision and control.
7. Miscellaneous matters such as indemnity, priority of sight and savings account liabilities and penalties on directors and managers.
8. Provision for consequential amendments that needs to be made to other related acts to enable Islamic banks to carry out their operations.

It is to be noted that the IBA only governs the Islamic banks. In other words, conventional banks that operate the Islamic banking business are not under the purview of this act.

2.6.1.2.3 Banking and Financial Institutions Act 1989 (BAFIA)

Pursuant to the CBM's policy in authorizing the conventional banks to operate Islamic banking business through Islamic windows, the Banking and Financial Institutions Act 1989 (BAFIA) was revised in 1996 in order to enable any conventional bank licensed under this Act to carry on with Islamic banking businesses or Islamic

[104] Islamic Banking Act 1983.

financial businesses provided that a prior consultation with the CBM for that purpose shall be made.[105]

Section 124 of BAFIA has been amended to facilitate the establishment of Islamic banking financial business in the conventional banks. The definition of "Islamic Banking Business" in Subsection 124 (7)(b) of BAFIA is the same as IBA. Therefore, this indicates that the nature of Islamic banking businesses by Islamic banks is the same design of the Islamic banking system implemented in the conventional banks. Under BAFIA, Islamic banking business has the same meaning as that in the IBA while Islamic financial business is defined in section 124(7)(c) as:

"... any financial business, the aims and operations of which do not involve any element which is not approved by the Religion of Islam".

Section 124(3) and (4) of BAFIA further provide that any licensed institution carrying on Islamic banking business or Islamic financial business may refer to CBM's SAC and shall comply with the directions on the Islamic banking business or Islamic financial business issued by the CBM in consultation with the SAC.

It should be noted that under section 124(5) of BAFIA, the licensed institutions under the Act are not Islamic banks but conventional banks offering IBF services. Formerly, these IBF services were known as "Skim Perbankan Tanpa Faedah" (SPTF) windows. At present, they are known as Islamic banking Scheme (SPI).[106]

2.6.1.2.4 Development Financial Institutions Act 2002 (DFIA)

In Malaysia, the Islamic financial institutions are governed under BAFIA and IBA acts. However, there are some banks that operate Islamic finance and they are governed under the Bank Rakyat Act 1978 and the Co-Operative Societies Act 1993.

---

[105] *Ibid.*, 203.

[106] Islamic Banking Malaysia, "Legal and Regulatory Framework of Islamic Banking and Finance in Malaysia," Islamic Banking Malaysia Website, retrieved on 1 July 2013, http://islamicbanking-malaysia.com/legal-regulations/170-legal-and-regulatory-framework-of-islamic-banking-and-finance -in-malaysia.

For example, the Bank Kerjasama Rakyat Malaysia Berhad. Although holding the name "bank" as in their title, it merely connotes as an institution offering financial and banking services whereby Bank Rakyat is just a co-operative institution.

Section 129 (1) of the Development Financial Institutions Act 2002 states: "Nothing in this Act or the Islamic Banking Act 1983 (Act 276) shall prohibit or restrict any prescribed institution from carrying on an Islamic banking business or Islamic financial business in addition to its existing business, provided that the prescribed institution shall obtain a prior written approval of the Bank before it carries on an Islamic banking business or any Islamic financial business."

Despite Bank Rakyat Malaysia Sdn. Bhd. as a development financial institution offering the Islamic banking services, there were also other development banks provided the same services such Export-Import Bank of Malaysia Berhad, Agro Bank, Bank Perusahaan Kecil dan Sederhana Malaysia Berhad (SME bank), and Bank Simpanan Nasional Berhad. All banks, which provided such services were governed under section 129 (1) of the DFIA act.

2.6.1.2.5 Central Bank of Malaysia Act 2009

The Central Bank of Malaysia Act was first enacted in 1958 and known as the CBA 1958. In 2009, the CBA 1958 had been repealed by the Central Bank of Malaysia Act 2009, which became effective on 25 November 2009. It provides for the continued existence of the Central Bank of Malaysia (the Bank), provides greater clarity to the Bank's mandates on promoting monetary and financial stability, and exercises oversight over payment systems. Drawing lessons from the global financial crises in the financial regulation, surveillance and crisis management framework and the need for effective coordination not only across sectors, but also across border, the CBA aims to adequately capture and pre-emptively address sources of risks to financial stability. In doing so, it vests the Bank with the necessary powers and instruments to achieve its mandates effectively. It also gives due recognition to the Islamic financial system in Malaysia by providing the legal foundation for its development in the overall Malaysian financial system.

With the enactment of the CBA, the Central Bank of Malaysia Act 1958 (except Part III) ceased to apply.[107]

Table 2.7: Islamic banking institutions operating in Malaysia:

	ISLAMIC BANKS
1.	AFFIN ISLAMIC BANK
2.	AL-RAJHI BANKING & INVESTMENT CORPORATION (MALAYSIA) BERHAD
3.	ALLIANCE ISLAMIC BANK BERHAD
4.	AMISLAMIC BANK BERHAD
5.	ASIAN FINANCE BANK BERHAD
6.	BANK ISLAM MALAYSIA BERHAD
7.	BANK MUAMALAT MALAYSIA BERHAD
8.	CIMB ISLAMIC BANK BERHAD
9.	HONG LEONG ISLAMIC BANK BERHAD
10.	HSBC AMANAH MALAYSIA BERHAD
11.	KUWAIT FINANCE HOUSE (MALAYSIA) BERHAD
12.	MAYBANK ISLAMIC BERHAD
13.	RHB ISLAMIC BANK BERHAD
14.	STANDARD CHARERED SAADIQ BERHAD
15.	PUBLIC ISLAMIC BANK BERHAD
16.	OCBC AL-AMIN BANK BERHAD
	INTERNATIONAL ISLAMIC BANKS
1.	UNICORN INTERNATIONAL ISLAMIC BANK MALAYSIA BERHAD
2.	PT. BANK MUAMALAT INDONESIA, TBK.
3.	AL-RAJHI BANK KSA
4.	DEUTSCHE BANK AG
5.	ELAF BANK B.S.C
	PARTIPATING BANKS IN ISLAMIC BANKING SCHEME
A.	DEVELOPMENT FINANCIAL INSTITUTIONS (DFIs) OFFERING ISLAMIC BANKING SERVICES
1.	BANK KERJASAMA RAKYAT MALAYSIA BERHAD
2.	BANK PERUSAHAAN KECIL DAN SEDERHANA MALAYSIA BERHAD (SME BANK)
3.	BANK PEMBANGUNAN MALAYSIA BERHAD
4.	BANK PERTANIAN MALAYSIA BERHAD (AGROBANK)
5.	BANK SIMPANAN NASIONAL BERHAD
6.	EXPORT-IMPORT BANK OF MALAYSIA BERHAD (EXIM BANK)
B.	INVESTMENT BANKS
1.	AMINVESTMENT BANK BERHAD
2.	ALLIANCE INVESTMENT BANK BERHAD
3.	MAYBANK INVESTMENT BANK BERHAD
4.	CIMB INVESTMENT BANK BERHAD
5.	KAF INVESTMENT BANK BERHAD
6.	MIDF AMANAH INVESTMENT BANK BERHAD

[107] Bank Negara Malaysia, "Administered Legislation," Bank Negara Malaysia Website, retrieved on 5 July 2013, http://www.bnm.gov.my/index.php?ch=en_legislation.

7.	OSK INVESTMENT BANK BERHAD
C.	COMMERCIAL BANKS
1.	CITIBANK BERHAD
2.	DEUTSCHE BANK (MALAYSIA) BERHAD

Source: Central Bank of Malaysia Website
(http://www.bnm.gov.my/index.php?ch=li&cat=banking&type=IB&sort=title&order=desc)

2.6.2 TAKĀFUL

The word *Takāful* is derived from an Arabic root word, which means guaranty, amenability or suretyship and responsibility. Therefore, the literal meaning of *Takāful* is shared responsibility, joint guarantee, shared guarantee, mutual undertaking and collective assurance. The function of *Takāful* is to promote interchangeable relationship and agreement of mutual help among members in a particular group.[108]

The main tenet of the Islamic Insurance system consists of two elements; mutual cooperation and *Tabarru.'* Both tenets are approved by many contemporary Islamic jurists, which embrace the elements of mutual guarantee, mutual protection and shared responsibility.[109]

The issue on the legitimacy of insurance was discussed in the Congress of Islamic Research in Cairo in 1965. Later, in 1976, the First International Conference on Islamic Economics reached a consensus where the conventional insurance for profit is contradictory to *Sharī'ah*. In 1985, the Islamic Fiqh Academy in Jeddah ruled that: "The contract of commercial insurance with a periodical fixed premium provided by the present-day insurance companies is a contract which is void and therefore, haram in accordance with the requirement of *Sharī'ah*."

Takāful system based on the co-operative model was first introduced in 1979 in Sudan. Then, *Takāful* system experienced development and evolution with the introduction of new Takāful model based on a commercial purpose named as *Tijari*.

[108] International Shari'ah Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations,* 504.
[109] Asif Ahmed Qureshi, "Analyzing the Sharī'ah Compliant Issues Currently Faced by Islamic Insurance,"
Interdisciplinary Journal of Contemporary Research in Business, Vol.3, No.5, (September 2011), 281.

This model was first introduced in Malaysia in 1984. This new model was accepted among *Takāful* companies worldwide rather than the mutual *Takāful* system. In fact, there are many issues triggered in the system. The current *Takāful* practice of *Tijari* model applies three main types namely; Profit-Sharing (*Mudhārabah*), agency model (*wakālah*) and hybrid model. Malaysia has implemented modified versions of *mudhāarabah* and *wakālah* models while other countries apply the latter model. [110] Thus, it could be concluded that, most worldwide *Takāful* operators apply the following models: [111]

Non-profit model: This model operates based on a purely mutual and co-operative system but without a consideration on the formal legal structure. The fund is managed by the board that represents all participants without the objective of targeting investment.

Commercial model: *Takāful* operator is given responsibilities in controlling *Takāful* fund. This must be conducted under specific rules of jurisdiction whereby the fund may be placed under the operator's management with a separation of two types of funds, namely

shareholders' and participants' funds. Another option, the fund may be set up as a company separated from the operator. The application of *Takāful* in other countries is through a window of a conventional insurer.

[110] Razaleigh Muhamat @ Kawangit, Abdul Ghafar Don, Salasiah Hanin Hamjah, Fariza Md.Sham, Badlihisham Mohd.Nasir, Muhammad Faisal Asha'ari, Siti Rugayah Tibek, Zainab Ismail, Ideris Endot, Anuar Puteh, A'dawiyah Ismail, Mohd Zulkipli Abd Ghani, "The Management of Takaful Business Models in Malaysia," *Journal of Advances in Natural and Applied Sciences*, 6(4): 561-564, (2012), 561.

[111] Islamic Financial Services Board (IFSB) and International Association of Insurance Supervisors (IAIS),
"Issues in Regulation and Supervision of Takaful (Islamic Insurance)," (Islamic Financial Services Board
(IFSB) and International Association of Insurance Supervisors (IAIS) Working Paper Series, August 2006),
5.

In terms of Family (life) *Takāful*, there are two portions of participant funds, namely *Takāful* fund which is set up to cover mortality risk and the other fund is investment fund for an investment portfolio.

2.6.2.1 *Takāful* Regulation in Malaysia

The Malaysian *Takāful* act was passed by the government of Malaysia in 1984. *Takāful* Act 1984 covered all *Takāful* regulations including the function of the *Sharī'ah* Advisory Council and also the operational standards of *Takāful*. The meaning of *Takāful* is clearly stated in section 2 of the Malaysian *Takāful* Act 1984 as "a scheme based on brotherhood solidarity and mutual assistance to the participants in the case of need whereby the participants mutually agree to contribute or donate for that purpose."[112]

The *Takāful* legislation requires that *Takāful* operator must set up a *Sharī'ah* supervisory council, which functions to advise the *Takāful* operator on its *Takāful* operations and to ensure that the operation of *Takāful* does not involve any elements contradictory to the *Sharī'ah*.[113]

The operational framework of Malaysian *Takāful* could be described as follows:

1. Participants contribute a sum of money into a common fund, which will be used to mutually assist the members against a defined loss or damage.
2. A *Takāful* operator is entrusted to manage the fund who runs the operation commercially as a business venture for profit.
3. Sources of income for the operator are from:-

    1. Profit from the investment of its shareholders' fund; agency/*Wakālah* fee;

    2. Share of investment profit of *Takāful* funds; and/or

[112] Laws of Malaysia, Takaful Act 1984, 10.
[113] Bank Negara Malaysia, *The Central Bank and the Financial System in Malaysia*, (Kuala Lumpur: Bank Negara Malaysia, 1999), 257- 258.

3. Surplus of the *Takāful* funds.

In addition, there are three levels of supervision and regulation to strengthen the *Takāful* industry which are: first, local jurisdiction, second, the Islamic Financial Services Board's (IFSB) standards and the third is the Core Principles of the International Association of Insurance Supervisors (IAIS).[114]

2.6.2.2 Malaysian *Takāful* Models

Generally, *Takāful* system consists of two different types, which are "General *Takāful*" and "Family *Takāful*." The General *Takāful* contract could be described as a short-term policy. In this contract, the participants contribute fund and as a return for this contribution, the *Takāful* operators is obliged to undertake the risk. On the other hand, the Family *Takāful* is offered for a long-term purpose to cover the participants in the long-term coverage such as *Takāful* coverage for children's education, their pension and compensation for dependents, among other things, in the event of death and disability.

There are several *Sharī'ah* compliant models that have been used as instruments to operate *Takāful* namely*; Mudhārabah* model, *Wakālah* model, Hybrid of *Wakālah* and *Mudhārabah* model and Hybrid of *Wakālah* and *Waqf* model.

Observing the Malaysian Islamic insurance practice, each company has the freedom to adopt whichever model appropriate to them as long as the model complies with the principles of the Islamic Transactional Legislation and is approved by the Central Bank of Malaysia. Under the pure *Mudhārabah* principle, participants will provide capital (by paying contributions) to be invested by *Takāful* operators (which play their role as entrepreneurs) and if there is any profit, it will be shared between both

[114] International Shari'ah Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations,* 508.

parties (participants and entrepreneurs) according to a pre-agreed ratio.[115] However this model raised issues and controversies.

Takāful operators in Malaysia have another option despite using *Mudhārabah* model in their *Takāful* product. This alternative product is known as *Wakālah* model, which is based on the agent-principal relationship. Via this model, the *Takāful* operator becomes as an agent representing the participants whereby the contributions submitted by the participants are deemed as fees. *Wakālah*-based *Takāful* model is more acceptable among the global *Takāful* operators as this model is more compatible and sustainable with less *Sharī'ah* issues compared to other model.

Recently, there is another new model that emerged in the *Takāful* industry. This model is based on the hybrid model combining *Wakālah* and *Waqf* contracts. It will probably be implemented among global *Takāful* operators in the near future. Currently, Malaysia remains to use *Wakālah* model in their *Takāful* products.[116]

2.6.2.3 RE-*TAKĀFUL*

Takāful industry experienced evolution and is presented with more diversification from its first appearance. Through many years of development, it has now emerged with a new type of *Takāful*, namely Re-*Takāful*. Re-*Takāful* functions are based on mutual assistance among the *Takāful* operators. Through this system, a group of *Takāful* operators become participants among them and contribute funds into Re-*Takāful* fund. In the case when a risk occurs, the *Takāful* fund will be used for the purpose of sharing the risk in specified categories if these exceed prudent underwriting limits.[117]

---

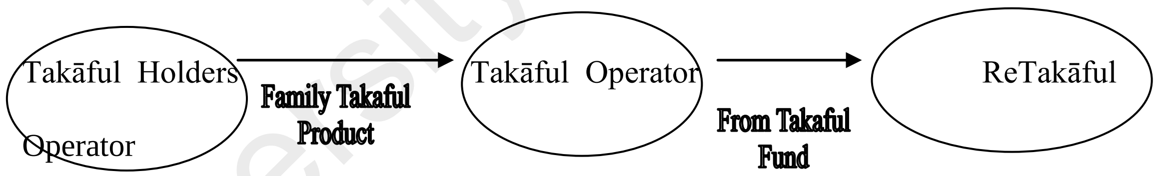
[115]Razaleigh Muhamat @ Kawangit, Abdul Ghafar Don, Salasiah Hanin Hamjah, Fariza Md.Sham, Badlihisham Mohd.Nasir, Muhammad Faisal Asha'ari, Siti Rugayah Tibek, Zainab Ismail, Ideris Endot, Anuar Puteh, A'dawiyah Ismail, Mohd Zulkipli Abd Ghani, "The Management of Takaful Business Models in Malaysia*," Journal of Advances in Natural and Applied Sciences, 6(4): 561-564, (2012),* 562.
[116] *Ibid.*
[117] International Shari'ah Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations,* 529.

The prime objective of the establishment of Re-*Takāful* is to become a risk aversion medium. Re-*Takāful* operates through the contribution among *Takāful* operators into the Re-*Takāful* fund whereby this fund will be used to compensate any unexpected future risks. This would be applied in the situation where the risk insured is more than the regular underwriting. Therefore, the *Takāful* reinsurance will take responsibility in covering an unexpected risk faced by *Takāful* companies using the *Takāful* Re-Insurance available fund.

Re-*Takāful* can also be described as "*Takāful* for *Takāful* operators." Eventually, it means a framework where a primary insurer responses to secure against unforeseen harms and losses.

Conventional Reinsurance plays the roles in controlling liability against certain risks, increasing individual insurers' capacity, sharing liability and favoring insurers to counterbalance their business in the case of the wide swings in profit and loss margin.

Diagram 2.3: *Takāful* and Re-*Takāful* Operation's Flow



Based on the above diagram, *Takāful* holders are individuals or companies, which purchase the *Takāful* products either General *Takāful* products or Family *Takāful* products and then pay an agreed-upon premium (contribution) to the *Takāful* operator for the security of unforeseen risk and also extraordinary losses. Later, the Takāful operator will use a portion of the *Takāful* fund to participate in the Re-*Takāful* scheme for protection in exceeded and unforeseen liability and to spread its risks. Re-*Takāful* contracts may cover a specific risk or a broad class of business.

Table 2.8: The List of Malaysian *Takāful* and Re-*Takāful* Operators

No.	Takāful Operators	Ownership
1	AIA AFG Takāful Bhd.	Foreign
2	AmFamily Takāful Berhad	Local
3	CIMB Aviva Takāful Berhad	Local
4	Etiqa Takāful Berhad	Local
5	Great Eastern Takāful Sdn. Bhd.	Foreign
6	HSBC Amanah Takāful (Malaysia) Sdn Bhd	Local
7	Hong Leong MSIG Takāful Berhad	Local
8	ING PUBLIC Takāful Ehsan Berhad	Foreign
9	MAA Takāful Berhad	Local
10	Prudential BSN Takāful Berhad	Local
11	Syarikat Takāful Malaysia Berhad	Local
12	Takāful Ikhlas Sdn. Bhd.	Local
	Re-Takāful Operators	
1	ACR ReTakāful Berhad	Local
2	MNRB ReTakāful Berhad	Local
3	Munchener Ruckversicherungs-Gesellschaft (Munich Re Re-*Takāful*)	Foreign
4	Swiss Reinsurance Company Ltd. (Swiss Re ReTakāful)	Foreign

Source: Bank Negara Malaysia Website (http://www.bnm.gov.my)

2.6.3 ISLAMIC FINANCIAL MARKET IN MALAYSIA

The establishment of the Islamic financial market in Malaysia was backed with a historical moment. Prior to the establishment of the Islamic financial market, the government had given focus to the Islamic banking sector as it became a pioneer for the Islamic finance in Malaysia, which offers Islamic deposit and finance services for the Muslim. The overwhelming support from Muslim depositors as well as non-Muslim resulted in an extraordinary liquidity issue for Islamic banks. This situation had brought a new problem when the bank's funds could not be mobilized and remained idle due to the limited investment opportunities since there was no *Sharī'ah* compliance market in that course of time.

As a result, there is no channel for Islamic banks to invest their exceed funds and reap the returns simultaneously. Unlike the conventional system, however, there are various financial instruments available to the surplus banks to invest any excess funds they have.[118]

In essence to the problems facing Islamic banks, the global Islamic banking system viewed that having its own financial markets was important for further

[118] Sudin Haron and Wan Norsofiza Wan Azmi, *Islamic Finance and Banking System: Philosophies, Principles and Practices*, 359.

growth.[119] As an introduction, the financial market normally pertains to the mechanism or the sector in which the financial instruments are transacted and the price of the instrument is determined by supply and demand. It serves as a channel of funds from units of surplus resources to deficit units in the economy. With the establishment of financial markets, it would benefit the community because they can enjoy a variety of channels and a variety of financing to meet their goals, whether medium-term loans or long-term loans. Financial market is also known as a communication mechanism to ensure an efficient conduit in a financial system for the conduct of its business. Financial markets must be organized, efficient and able to provide the facilities required by the customer including the distribution system and an effective trading system as well as efficient in conducting market instruments. It should also have risk management facilities and is able to offer various instruments for the purpose of reducing the risk.[120]

The Islamic finance scholars realize the importance to establish an Islamic financial market and started to ponder the possibility to set up the model of an Islamic financial market and its mechanism. For this purpose, the development of an Islamic financial market instrument is vital so it could become as an alternative to the conventional counterpart. This financial instrument must, however, possess the following features of conventional financial instruments:

i) They must be negotiable, that is, it must be easy to transfer the ownership of the instruments from one holder to another.

ii) They must be liquid, that is, they can be easily sold when cash is required.

iii) They must carry minimum risk.

iv) They must be easily valued and priced.

Since Islamic financial markets are at its developing phase, these new concepts have raised numerous theoretical and practical debates. The issue of religious rules

[119] *Ibid.*
[120] Abdul Mumin Ab. Majid and Fadillah Mansor, *Dinamisme Kewangan Islam Di Malaysia*, 15.

(*hukum*) also occasionally causes confusion and a continuous debate not only among the local intellectuals, but also among countries.[121]

The Securities Commission in Malaysia plays a role in governing the financial market matters. As mentioned earlier, the Securities Commission Malaysia (SCM) was established on 1st March 1993 and governed under the Securities Commission Act 1993. The SCM functions as a single regulatory authority and is responsible for the structured development of the capital market as well as broader issues including investor protection.

In order to highlight a clear strategic path for the future objective of SCM, one master plan named as the capital market master plan was issued in 2001. This ten-year integrated plan provides a clear direction for the function of the SCM within the 10 years.[122]

2.6.3.1 Types of Financial Market

The structure of a conventional financial market comprises four components, namely capital market, money market, futures market and mortgage market. The capital market trades instruments with an original maturity of more than one year. The money market transacts in short-term financial instruments whose maturity period is one year or less. The mortgage market covers real estate financing (e.g. financing of homes, buildings and other properties. The forward and futures market involves a contract between two parties for future delivery of currencies, securities or commodities.[123]

Nevertheless, the implementation of full financial market components is not necessary to be formed inside the country's financial market. Ignoring the situation in a

---

[121] Sudin Haron and Wan Norsofiza Wan Azmi, *Islamic Finance and Banking System: Philosophies, Principles and Practices,* 359.

[122] Securities Commission of Malaysia, Capital Market Development in Malaysia: History and Perspectives, Kuala Lumpur, 2004.

[123] Sudin Haron and Wan Norsofiza Wan Azmi, *Islamic Finance and Banking System: Philosophies, Principles and Practices,* 361.

developed country, the establishment of the financial market components depends on the country's level of economic development.[124]

The Islamic system may not have all four types of the financial market components as what the conventional market has. The Islamic financial market comprises the Islamic money market and the Islamic capital market.

2.6.3.2 Islamic Capital Market and its Practice in Malaysia

The capital market is commonly known as a place for the issuance and the trading of the long-term financial instruments with the maturity of more than one year. The objective of the establishment of the SCM is to manage savings and channel it into long-term productive investments. Various parties are involved in the transactions and business of the SCM including the government and the private sectors.[125]

The capital market caters for a long-term financing where the length of maturity in the capital market normally used to exceed more than 12 months. The financial instruments in the capital market vary, which includes sukuk, bonds and equities. Transactions in capital market instruments are either exchange, traded or OTC (Over the Counter).

In the capital market, the financial instruments could be divided into two types, namely equity instruments and debt instruments. As a basic understanding, equity instruments come with share certificates whether in the form of common or preferred stocks. Debt Instruments could be described as bonds which consist of common bonds and convertible bonds. The difference between stocks and bonds lies in their payment of returns (either in the form of dividend or interest) to the owner or holder.[126]

---

[124] *Ibid.*
[125] *Ibid.*
[126] *Ibid.,* 362.

The dissimilarity between common stock and preferred stock rests on the dividend payment. The payment of dividends for preferred stock is generally in the form of a fixed percentage and it takes priority over common stock dividends. For common stock, dividends paid depend entirely on the discretion of the Board of Directors. In addition, preferred stockholders have a claim prior to common stockholders on the company's assets. Preferred stock consists of two types, namely cumulative and non-cumulative.

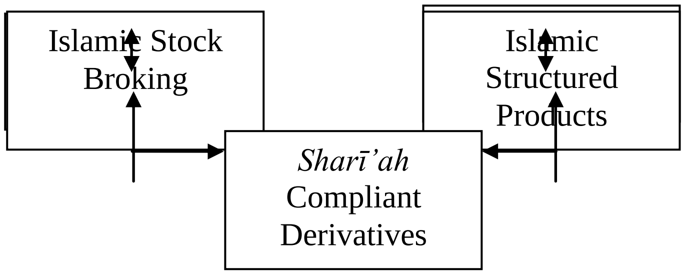
There is non-*Sharī'ah* compliance in common stock and preferred stock, which makes this instrument invalid to Muslims and Islamic banks. As a basic understanding for this prohibition, the preferred stock comes with pre-determined fixed rate of return, which does not comply with *Sharī'ah*. Nevertheless, there is a way out from involving with this transaction where Islamic scholars proposed that preferred stocks might be issued by using the concept of a preference dividend based on a pre-determined profit ratio. As long as the practice of profit ratio method is exercised without the fixed payment, the preferred stock using this concept is allowable in *Sharī'ah*. In sum, the preferred stockholders have no knowledge of the amount of annual dividends belong to them and the calculation of dividends based on the profits gained by the company.[127]

Under *Sharī'ah*, the concept of common ownership is permissible. Therefore, it is legal to undertake sale, pawning or donation. During the process of buying and selling stocks, what changes is only the ownership right and it is this exchange of value that is paid using cash or other modes of payment.[128]

Islamic scholars have approved four types of Islamic capital market instrument, namely Islamic equity market, *Sukuk* market, Islamic Stockbroking and Islamic Structured product. Diagram 2.4 shows a brief picture of the Islamic Capital market.

[127] *Ibid.*
[128] *Ibid.,* 364.

Diagram 2.4: Capital Market framework



2.6.3.3 *Sukuk* Market

Sukuk is counted as a vital and prime element of an Islamic capital market. The transaction of *Sukuk* represents about 90% of the Islamic capital market system. The types of financing in *Sukuk* market consist as follows:

2.6.3.3.1 Islamic Asset-Based Financing

Islamic financing is based on the sale and purchase of assets. In this regard, it differentiates itself with the conventional counterpart. Underlying asset will first be acquired by the bank, prior to the financing provided through the sale and purchase of assets. In Islam, the money is a medium of transaction to complete the transaction. This is not always the case with the conventional finance in which most of the time the financing is currency-based.

2.6.3.3.2 Islamic Equity-Based Financing

The model of Islamic equity-based financing is formed under the concept of risk sharing in the business. The term share connotes the meaning of sharing between both parties in the business venture such as sharing in capital, management, the technical expertise, labors or any matters related to professional attributes. The distribution of profits must be as agreed in the beginning of the contract while losses are prorated to each party's capital participation. The equity financing will be exercised after proceeding into one of two contracts, namely a partnership contract and a trust-financing contract.

2.6.3.3.3 Islamic Asset-Backed Securities

The function of *Sharī'ah* compliant asset-backed securities (ABS) is to deliver risk-return profile, which is applying the same practice in the conventional system. Islamic Asset-Backed Securities could be described as debt securities that involve underlying assets or real estate. This includes receivables, financings, leases, royalties, etc. It differs from the conventional one in which the conventional securitization was developed based on interest-bearing debt.

2.6.3.4 Islamic Equity Market

Islamic Equity market operates on the basis of equity participation by the investor. It includes the following Islamic products:

- *Sharī'ah* -compliant stocks
- Islamic Unit Trust
- Islamic REIT's (Real estate investment trusts).
- Islamic Index.

Equity-based contract involves a partnership and the sharing of risks and rewards in a venture. Islamic contracts based on the Sharing concept are *Mudhārabah* and *musharakah*. Profits from this contract are gained from capital yields by selling the purchased shares or securities at higher prices. Profits can also be obtained through dividends, at the time of profits distribution by the issuing companies.[129]

[129] International Shari'ah Research Academy for Islamic Finance (ISRA), *Islamic Financial System: Principles and Operations,* 452.

Secondary market trading of shares is approved by Islamic scholars who advocate one of the two approaches; 1) shares as reflecting partnership interest and 2) shares as ownership of enterprise.

In accordance to the equity valuation, there is yet any Islamic valuation framework. The current practice of valuation is based on the conventional method. However, the valuations are accepted among Islamic scholars as long as securities can be declared as *Sharī'ah*-compliant through some kinds of *Sharī'ah* screening by various jurisdictions.

The Islamic Equity Market Instruments comprises of Shares of Stocks (preference shares, Stock Index Futures, Short-Selling), Unit Trusts or Mutual Funds, Islamic Real Estate Investment Trusts (REITs) and Islamic Exchange Traded Funds.

In June 1997, the *Sharī'ah* Advisory Council (SAC) of the Securities Commission Malaysia announced the list of Approved Securities is 371 or 57% passed the *Sharī'ah*. The SAC uses certain criteria especially for making in-depth study towards major activities of companies listed on Bursa Malaysia and MESDAQ.[130]

Approved securities refer to the normal activities exercised by the company, which does not breach the *Sharī'ah* principles. In the situation where prohibited activities like gambling, usury, *gharar* take place in certain businesses, such company will be automatically banned from the approved securities lists.[131]

2.6.3.5 Islamic Structured Products

Islamic structured investment products are customized products subject to the request of a specific investor who can be a wealthy individual or a group of investors. The risk and reward of these products are designed to meet a specific objective. Commonly, the following two types of Islamic structured products are practiced in the Islamic capital market:

[130] Abd. Mumin Ab. Ghani and Fadillah Mansor, *Dinamisme Kewangan Islam Di Malaysia* , 17.
[131] *Ibid.*

- Dual currency structured Investment

- Equity Linked structured Investment

The Malaysian capital market and services act 2007 defines "structured product" as "any investment product that falls within the definition of "securities" under the SCA and which derives its value by reference to the price or value of an underlying reference."[132]

Section 2.04 provides that the *Sharī'ah* principle (s) and concept (s) adopted for an Islamic structured product must be based on the principles and concepts approved by the SC's *Sharī'ah* Advisory Council (SAC), a list of which is mentioned in Appendix 2.[133]

2.6.3.6 Islamic Stock Broking

In an Islamic capital market, stock broking is conducted according to the *Sharī'ah* principals. This part of an Islamic capital market deals in the following:

- *Sharī'ah* -compliant trading
- *Sharī'ah* -compliant margin financing

In Malaysia, an Islamic stockbroking is classified as a participating organization, which provides beginning-to-end compliant stock. It is designed to serve as an agent on behalf of the clients to buy or sell *Sharī'ah*-compliant equities based on a wall contract. In the current practice, the *Wakālah* contract is applied in two-tier agency contracts: the first layer of *Wakālah* is between the client and the Islamic Stockbroking firm while the second layer is between the Islamic Stockbroking firm and Bursa Malaysia.[134]

2.6.3.7 *Sharī'ah* Compliant Derivatives

---

[132] Guidelines on the Offering Structured Product, Securities Commission of Malaysia, Revised Edition: 27 April 2007, 1.

[133] *Ibid.*, 2.

[134] Mohammad Mahbubi Ali, "Stockbroking in Islam: A Review of Literatures and Its Future Development in Malaysia," (Business & Management Quarterly Review, 3(3), 1-8, 2012), 4.

The current practice of derivatives involves hedging application where hedging functions as an offsetting position with the objective to balance gains and losses towards an underlying asset. Hedging is exercised to stabilize volatility resulted from an uncertainty in the price of an asset by taking offsetting positions in the contrary to what the customer currently has. Hence, derivative could be defined as a financial instrument which value depends on the value of other; for examples, basic variables items such currencies, indexes, palm oil, crude oil and grains. Derivatives instruments could be divided into four types as follows:[135]

1. Forward
2. Futures
3. Options
4. Swap Contracts

2.6.3.7.1 Forward

In the derivative system, forward contract is considered as the first instrument applied in the system, which is viewed among the practitioners as the simplest one. The implementation of a forward contract begins between two parties when they complete a transaction to be made on a future date with the price being predetermined during the present transaction.

Basically, the Islamic Fiqh Academy in its seventh session in 1412 H (9 to 14 May 1992) has made a resolution that forward contract is not permissible because of the deferment of the two elements of the exchange. However, it may be amended to meet the well-known conditions of "*Salam*" (advance payment). If it does so, it shall be permissible.

[135] International Shari'ah Research Academy for Islamic Finance, *Islamic Financial System: Principles and Operations,* 590-591.

Based on this ruling, the Islamic scholars reached a consensus to allow such an Islamic-compliant forward contract, which is named as the Forward *Wa'd* – I contract. The product is based on the unilateral contract with the involvement of two parties. The flow of contract begins with the first party giving a promise to the second party to buy or sell currency for a settlement on a forward value date based on today's rate and amount as agreed. The first party as the party who gives the promise is obliged to honour the contract, but the second party is not obliged to do the same.[136]

2.6.3.7.2 Futures

A futures contract is also known as a standardized forward contract, which requires certain conditions like contract size, maturity, product quality and other related conditions. The way of trading futures contract is through the exchanges of deals, which becomes a mediation of all buyers and sellers. A number of buyers and sellers are transacting the exchange in which this brings into a solution against the problem of multiple coincides. From the Islamic perspective, futures contract is forbidden due to its nature as a type of sale of one debt for another.

2.6.3.7.3 Options

An option contract is a contract where the holder entitles to the right, but not the obligation, to buy (or sell) the underlying asset at a pre-determined exercise price at any time before maturity. Initially, to obtain this right under an option, a premium payment is required. There are two basic types of options: a call option and a put option. A "call option" provides the holder the right to buy while a "put option" provides the holder the right to sell the underlying asset at a pre-determined price.[137]

The OIC Islamic Fiqh Academy when holding its seventh session in 1412H (9 to 14 May 1992), Resolution No. 63/1/7 stated:

[136] *Ibid.,* 605.
[137] *Ibid.,* 591.

“Option contracts as currently applied in the world financial markets is a new type of contract which does not come under any one of the *Sharīʼah* nominated contracts. Since the object of the contract is neither sum of money nor a utility or a financial right which may be waived, then the contract is not permissible in *Sharīʼah*.”[138]

Islamic scholars extensively reviewed the option contract in order to screen *Sharīʼah* compliance matter in the contract. After having some amendments, the Islamic scholars had approved Forex *Wa'd* Islamic contract. The Forex *Wa'd* is a structure that is very similar in formation to the conventional option. It uses the *Wa'd* promise, which is binding on one party. On the start date of the transaction, the bank will undertake that the customer exchanges Currency 1 against Currency 2 at a pre-agreed rate on a future date. On the same date, the bank will receive a fee from the customer for its undertaking.[139]

2.6.3.7.4 Swaps Contracts

In conventional financial swaps, there are various types of swaps, namely the interest-rate swap, commodity swap, currency swap and equity swap. A swap contract is an underlying-based contract. It could be described as an agreement between two parties to exchange payments in an agreed period based on the value of the underlying asset. The rate of money during the exchange payments is pre-determined via two methods of either based on a fixed amount or based on a reference measure.[140]

Within the Islamic finance perspective, swap trading includes speculation and verges on *maysir*, *qimar* and *gharar*. Therefore, the swaps contract is not permissible in Islam. Hence, the Islamic scholars have made modification and screening on the

[138] IRTI, Resolution and Recommendations of the Council of the Islamic Fiqh Academy: 1985-2000, Islamic Development Bank, Jeddah, Saudi Arabia: 131.
[139] International Shari'ah Research Academy for Islamic Finance, *Dinamisme Kewangan Islam Di Malaysia*, 609.
[140] *Ibid.,* 592.

contract and had endorsed the Islamic Profit Rate Swap, Islamic Cross Currency Swap (ICCS) and Islamic Forex Swap.

2.6.3.8 Islamic Money Market and Its Practice in Malaysia

The functions of the money market are most importantly to provide an efficient means for economic units in the economy to adjust their liquidity positions. Financial instruments in this market have three crucial features namely, short term to maturity, low default risk and high marketability. In the conventional money market system, the most widely traded financial instruments are treasury bills, negotiable certificates of deposits, banker's acceptance and repurchase agreement.[141]

Many parties are involved in the money market transactions such as banks and non-banks, financial institutions like *Takāful*, insurance companies, business corporations, central bank and government treasury. The objective of using this facility by the banks is to liquidate its assets, in primer to make adjustment for a mismatch asset and liability in the bank's balance sheet. In summary, banks will use the money market for liquidity or to place surplus funds over a limited period.[142]

The Islamic money market is the best place where the money market players invest surplus funds or to obtain short-term funding in a *Sharī'ah*-compliant way. Similarly, the players are allowed to trade in *Sharī'ah* -compliant money market instruments as well as to carry out *Sharī'ah*-compliant hedging facilities.

Initially, the financial instruments in the Islamic money market have not really spread out to Muslim countries. However, Malaysia has taken an effective effort to pave the way by providing *Sharī'ah*-based financial instruments for negotiation in the money market. In 1994, the first Islamic inter-bank money market was established in Malaysia, which consisted of three main components, namely inter-bank trading in Islamic financial instruments, Islamic inter-bank investments and inter-bank cheque clearance

[141] Sudin Haron and Wan Nursofiza Wan Azmi, *op.cit,* 375.
[142] International Shari'ah Research Academy for Islamic Finance, *Dinamisme Kewangan Islam Di Malaysia,* 354.

system. However, in 1999 when consolidation took place in the cheque clearance system, RENTAS (Real Time Electronic Transfer of Funds and Securities), the Islamic inter-bank cheque clearance system ceased to be regarded as a component of the Islamic inter-bank money market. At present, the Islamic inter-bank money market is made up of two components only, namely the inter-bank trading of Islamic financial instruments and the Islamic inter-bank market.[143]

In the Islamic money market instruments, trading represents the second component of the Islamic money market. Its objective is to facilitate the placement among the money market players similar to the interbank investment, but through the issuance/purchase of financial instruments. The money market instrument is more flexible compared to the above interbank investment in the sense that the instruments can be easily traded in the secondary market. Thus, this makes it easy for banks that buy money market instruments to sell or liquidate them in any intention without having to wait for the maturity of the instruments. An active secondary market is, therefore, capable of facilitating the trading of money market instruments prior to maturity. Such trading reduces liquidity risk and enhances market efficiency.[144]

The Islamic instruments exercised in the Malaysian Islamic money market trading are such as the Government Investment Issues (GIIs), Malaysian Islamic Treasury Bills (MITBs), Bank Negara Monetary Notes (BNMNs), Sukuk Central Bank of Malaysia *Ijarah* (SBNMI) and Islamic Negotiable Instruments (INIs). The INIs may be issued based on *bay' bithaman ajil* or *Mudhārabah*. The instrument such as Negotiable Islamic Debt Certificate (NIDC) is based on *Bai' Bithaman Ajil* while the Islamic Negotiable Instrument of Deposit (INID) is based on *Mudhārabah* . Other

[143] Sudin Haron and Wan Nursofiza Wan Azmi, *Islamic Finance and Banking System: Philosophies, Principles and Practices*, 376-377.
[144] International Shari'ah Research Academy for Islamic Finance, *Islamic Financial System: Principles and Operations*, 371.

instruments are Sell and Buy Back Agreement (SBBA) and Cagamas Sukuk, which consist of *Sanadat Mudhārabah* Cagamas (SMC) and *Sanadat* Cagamas.

In the Islamic money market, the Islamic Interbank Market is generally considered as the largest component and in particular, in the overnight sub component. An active interbank market is essential in providing indications to central banks to ascertain the volume of open market operations. The overnight market is where the IFIs trade their reserve balances among themselves to meet their day-to-day liquidity requirements. For example, banks with surplus liquidity can place their surplus funds with other banks overnight. The overnight rate adjusts to balance the supply of and demand for bank reserves. A short-term market rate, in particular the interbank overnight rate, may function as an operational guide for monetary operations for central bank.[145]

The Islamic money market operates based on the *Mudhārabah* contract and consists of three types of instruments, namely Islamic financial instruments, *Mudhārabah* Interbank Investment (MII) and the check clearing system in Islam. Islamic banks and banks that adopt Islamic banking system (Skim Perbankan Islam (SPI banks)) are allowed to trade in financial instruments such as the Islamic accepted bills, Islamic bonds, short-term notes and bonds *Mudhārabah* Cagamas Islamic.

Surplus Islamic banks and SPI can invest through MII mechanism in Islamic banks and SPI banks that lack of funds based on the concept of *al-Mudhārabah* .[146] Malaysia IIMM also applied *murabaha* (commodity deposit) and *wakala* (agent representation) concepts in its product as a tool in liquidity management.

At present, the international practices of the Islamic interbank money markets are based on the s *Sharī'ah* concepts of *Mudhārabah* (partnership), *murābaha* (commodity deposit), *mushāraka* (joint venture) and *wakāla* (agent representation).

---

[145] *Ibid.*, 362.
[146] Abd. Mumin Ab. Ghani and Fadillah Mansor, *Dinamisme Kewangan Islam Di Malaysia*, 15.

2.7 FUTURE ISLAMIC FINANCE IN MALAYSIA

2.7.1 Malaysia as an International Islamic Financial Centre

The initiative of Malaysia to be an Islamic finance global hub has become as the government's objective and appeared as a national agenda. At the first stage of this effort, Malaysia, has extremely amended its Central Bank Act to recognize a dual (Islamic and conventional) financial system and has taken significant changes on other numerous legislatives and regulatory bodies in order to accommodate this vision. The vision to make Malaysia as a global Islamic finance hub is clearly stated in the Central Bank Act.[147]

60.(1) The Bank shall, in co-operation with the Government or any Government agency, statutory body, supervisory authority or international or supranational organization, develop and promote Malaysia as an international Islamic financial centre.

(2) For the purposes of subsection (1), the Bank may—

(a) Establish a secretariat or other committees to assist the Government or any organization, council, agency or committee established by the Government; and

(b) Generally, take such measures or facilitate such actions or provide financing, as may be necessary for the development and promotion of Malaysia as an international Islamic financial centre.

The process of legal and regulatory changes is not as simple as thought. The existing legal and taxation systems have been developed over the years to accommodate the requirement of business formation and financial transactions and activities. The changes, however, have been made to facilitate the Muslim's domestic market with the futuristic plan to extend the Islamic finance system to stand in line with the conventional system.

[147] Laws of Malaysia Act 701, Central Bank Act 2009, 53.

In the year 2000, a 10-year development Master Plan for Malaysia's financial sector and capital market has been set up by the CBM and SC. The plan drafted the strategic guidance for the country's Islamic finance sector. In late 2006, the Malaysian International Islamic Financial Centre (MIFC) was set up by the Government and various financial regulatory bodies to transform Malaysia into a vibrant, innovative and competitive Islamic financial hub.[148]

2.8 CHAPTER SUMMARY

Overall, this chapter studies the Islamic finance system background in Malaysia. Ample explanations were given on the system which includes the regulator's framework, the Islamic finance product, the Islamic finance sectors namely Islamic banking, *Takāful* and the Islamic financial market. The Islamic banking and finance system in Malaysia experienced a very long journey to become as a sustainable system and nowadays successfully emerges as an alternative system to the conventional financial system counterpart.

The comprehensiveness of Islamic finance in Malaysia nowadays is a result of a highly collaboration of many parties include the Malaysian government, the Central Bank of Malaysia, the Islamic finance institutions and not least the Muslim communities in Malaysia which give a full support for the success of Islamic finance in Malaysia. The Islamic finance scholars in Malaysia also have given a significant contribution in the success of Islamic finance in Malaysia which among others provide professional *Sharī'ah* views and consultation in developing the Islamic finance products, screening and reviewing non-*Sharī'ah* products, conduct researches in many areas with the objective to develop Islamic finance as a robust system as can be seen in the current century.

[148] PricewaterhouseCoopers, *Malaysia, Asia's Islamic Finance Hub, PricewaterhouseCoopers (PwC),* (Kuala Lumpur, Malaysia: PricewaterhouseCoopers, 2008), 15.

CHAPTER THREE

THE GLOBAL HUB PROCESS: MALAYSIA’S VISION TOWARDS BECOMING AN ISLAMIC FINANCE GLOBAL HUB COUNTRY

3.0 INTRODUCTION

The idea of Islamic finance global hub could steer the development of Islamic finance in Malaysia due to the enhancement of financial service quality for local and global customers. The global hub concept has a connection with financial liberalization, which is a part of globalization. Therefore, the study on Islamic finance global hub will also include the elaboration on financial liberalization within the context of globalization. This chapter attempts to explore the Islamic finance global hub process in a country. This chapter is expected to answer the second problem statement as highlighted in the first chapter.

First and foremost, it is important to understand the interpretation of globalization is due to its connection with financial liberalization and the global hub agenda. The International Encyclopedia of Business and Management defines globalization as “the process of increasing integration of world civilization.” On the other hand, the Oxford Dictionary of Business defines globalization as “the internalization of products and services by large firms.” Historically, the term "globalization" was first used in 1985 by Theodore Levitt to describe the immense changes that had taken place over the last two to three decades in the international economy. That is, the rapid changes in economy and finance that have taken place in capital, production, consumption and investment of goods, services and technology across the world. The best description of globalization appeared by the widening and deepening of international flows of trade, finance and information in a single integrated global market.[149] There are several debates on the definition of globalization. The understanding of globalization from its origin and the current definition might have a different connotation. There might be a different connotation in the understanding of globalization from its origin and the current definition. In certain contexts, the term globalization may be understood as an internationalization or multinational, which meaning of the two terms is interchangeable while in different contexts the term globalization connotes a different meaning. Therefore, the exact definition of globalization and how it really works is still a debate among scholars. Based on the contemporary scholars' discussion, globalization means different things to different people.[150] According to Albrow, "Globalization refers to all those processes by which the peoples of the world are incorporated into a single world society, global society."[151] Gibbons: "One cannot conclude that if globalization has not occurred it is not a process. It may simply be that globalization is proceeding in a very uneven fashion and that trends which can be readily discerned in financial systems to some extent in research and development, particularly in the electronics industry, ought not to be presumed to apply same degree in every sector." [152] Urry: "Globalization could be viewed as the replacing of one region, the bounded nation-state society of the 'west,' with another, that of global economy and culture. Globalization could also be viewed not as involving alternative metaphors of network and fluid."[153]

The New Palgrave Dictionary of Economics[154] elaborated on globalization debate, which it is about a surprisingly large number of issues, including some that lie

---

[149] David Brian Dewitt and Carolina G. Hernandez, *Development and Security in Southeast Asia: Globalization*, Vol.3, (England: Ashgate Publishing Limited, 2003), 234.
[150] *Ibid.*,243.
[151] Martin Albrow and Elizabeth King, *Globalization, Knowledge and Society*, (London: Sage Publications, 1990), 9.
[152] Gibbons, M. et al., *The Globalization of Higher Education*, (Buckingham, UK: The Society for Research into Higher Education and Open University Press, 1998), 70-87.
[153] John Urry, *Sociology Beyond Societies, Mobilities for the twenty-first century*, (London: Routledge Publication, 2000), 191.
[154] The New Palgrave Dictionary of Economics, vol. 3, Second Edition, (New York: Palgrave Mcmillan Publishers Ltd., 2008), 681.

outside of economics. A non-exhaustive list of issues, derived from a reading of the writings of both economists and non-economists are as follows:

1. Liberalization versus regulation of international trade, capital movements and migration.
2. Market imperfections that arise with (either domestic or international) goods markets, capital markets, privatization, macroeconomic crises, intellectual property rights, and so on.
3. Evaluation of the performance of the International Monetary Fund (IMF) and the World Bank, including in particular, their policy prescriptions (the 'Washington Consensus,' 'shock therapy,' or 'Structural adjustment').
4. Effects of freer trade and capital movements on rich country workers ('out-sourcing') and on poor country workers ('sweatshops').
5. Extreme world inequality and poverty.
6. Capitalism ('neoliberalism') versus alternative systems.
7. Westernization/ Americanization versus local culture.
8. Unequal distribution of political power between the West (both Western government and corporations) and the Rest.
9. Effect of global economic growth on the environment.
10. Western imperialism and military intervention in the rest of the world.

However, both the theoretical and empirical of globalization were derived from the economic argument debated by Levitt. Richard S. Tedlow and Rawi Abdelal[155] who studied the intention of Levitt from his word "globalization." The study found that from

[155] Richard S. Tedlow and Rawi Abdelal, "Theodore Levitt's The Globalization of Markets: An Evaluation after Two Decades," (Social Science Research Network Electronic Paper Collection (No. 03-
20), 2003), 22.

Levitt perspective, “globalization” is a concept appreciated beyond the increase in economic exchange across borders; it refers to a change in the character of those exchanges across borders; which transforms the societies involved into the exchange. Thus, it is important to understand the distinction between “internationalization” and “globalization” in which both have a different meaning. This is due to the similarity of both in size and expansion of markets where it represents the world of economic interdependence of societies living in various countries.[156] Hence, the term "globalization" portrays a situation where an economic activity is running in the absence of national boundaries. The term "internationalization" implies an additional transaction across borders of a nation's states, which are still under control by the governments that have a decision option over the openness of global corporations operating in a globalized economy, while multinational corporations expanded in a sphere of internationalized economy. In a similar view, Herman E Daly[157] agreed on the difference between internationalization and globalization. According to Herman, the term "internationalization" connotes the increasing of international trade, international relations, treaties, and alliances. The term International literally means between or among nations. The basic unit remains that the nation becomes necessary and important. Globalization transformed many formerly national economies into one global economy based on a free trade and free capital mobility by eliminating national boundaries for economic purposes. International trade (governed by comparative advantage), therefore, becomes an interregional trade (governed by absolute). What was many becomes one presently.[158] David Brian Dewitt and Carolina G. Hernandez, also have a similar view with prior researchers as reflected in their point: “globalization

---

[156] David Brian Dewitt and Carolina G. Hernandez, *Development and Security in Southeast Asia: Globalization,* ed., England: Ashgate Publishing Limited, 2003), 234.
[157] Herman E. Daly, “*Globalization Versus Internationalization – some implications*,” *Journal of Ecological Economics 31*, (Elsevier Science (1999)), 31.
[158] *Ibid.*

means the internationalization of the state." They concluded that, "it is not surprising that the most common usage of the term "globalization" refers to the process of opening up the national economy and its integration into the global economy."[159] Such definition means that globalization is derived from internationalization which later on expands to the wide global economy.

Globalization may have both positive and negative effects. Perhaps, the issue may arise on the effectiveness of a government's control towards negative effects via certain policies for the nation's benefit and value for the globalization's agenda.[160] Positive views of globalization claim that the policy may increase economic growth and prosperity, without any doubt, where it would foster a country's growth when the country is properly positioned to take advantage from it, through sound institutions and policies. However, the negative views of globalization claim the negative effect is for everyone, no matter what policies and institutions are embraced. In addition, some insist that globalization affects the income inequality between countries while others view an adverse impact on income equality within countries. It may also increase global poverty. This is due to the globalization itself encompassing all.[161]

Hossein Askari, Zamir Iqbal and Abbas Mirakhor suggest that globalization is a new system, which is an ongoing process with far journey to be "complete" but it is not monotonic and could be reviewed. The impact of globalization is multidimensional. Some portion of society will gain while others will lose, or at least there will be unequal shares between the gain and the loss.[162] The potential benefit of globalization depends on how well a country is organized, its competitiveness in global goods and services markets, the flexibility of its markets and its policy and regulatory infrastructure.

---

[159] David Brian Dewitt and Carolina G. Hernandez, *Development and Security in Southeast Asia: Globalization,* 235.

[160] Hossein Askari, Zamri Iqbal and Abbas Mirakhor, *Globalization & Islamic Finance: Convergences, Prospects & Challenges,* (Singapore: John Wiley & Sons (Asia) Pte.Ltd., (2010), 7.

[161] *Ibid.,* 10.

[162] *Ibid.*

Therefore, all countries have to develop strong economic and social policies, the appropriate regulatory and supervisory environment, flexible markets, financial stability and the needed institutions to benefit from globalization, while guarding the economic welfare of all segments of society and preventing social and economic upheavals by increased access to education, healthcare, labor training and the like.[163]

3.1. THE CONCEPT OF FINANCIAL GLOBALIZATION

The globalization concept has an interconnection with economy and capitalism. These characteristics appeared in international trade liberalization, free movement of capital and transition between the states. Similarly, the presence of foreign direct investment flows to the developing countries and the dominance of the multinational companies in the country and the growth of economic blocs such as the European Union and the Southeast Asia's bloc (ASEAN).[164]

In financial services, globalization can be seen as a process of opening up national economies and markets. Mervyn K. Lewis[165], Hossein Askari, Zamir Iqbal, Abbas Mirakhor[166] and Mohamed Salim al-Rowashdah[167] view that globalization portrayed a situation of ease and speed of knowledge, technology, people, ideas, goods and services and capital move and transfer from country to country, thus, broadening the extent and form of cross-border transactions and growing the international character of economic activity. This trend is steered to achieve higher returns and more options to diversify risks. It is useful to succeed current international financial environment with

---

[163] *Ibid.*

[164] Mohammad Salim al-Rowashdah, "The Political and Financial Implications of Globalization on the Islamic Banking: Facts and Events*,"* *European Journal of Social Sciences* (Volume 12, Number 2, 2009), 185.

[165] Mervyn K. Lewis et al., *The Globalization of Financial Services*, (Cheltenham, United Kingdom: Edward Elgar Publication, 1999), xv.

[166] Hossein Askari, Zamir Iqbal and Abbas Mirakhor, *Globalization & Islamic Finance: Convergence, Prospects & Challenges*, 177.

[167] Mohammad Salim al-Rowashdah, "The Political and Financial Implications of Globalization on the Islamic Banking: Facts and Events,*"* 185.

increased uncertainties through more pronounced prompting of investor's venture into new asset classes and markets that provide stability.[168] While the economic and financial globalization is formed by different force of factors, economic and financial globalization shares a symbiotic relationship; they go together and reinforce one another.[169]

There are many studies conducted to examine the effect of financial liberalization. Some study suggests that, by promoting cross-country risk-diversifications, financial liberalization could foster specialization, efficiency in capital allocation and growth.[170] Some studies (e.g., Grilli and Milesi-Feretti,[171] Kraay,[172] and Rodrick[173]) found that financial liberalization does not affect growth, other than the effect is positive (Levine,[174]Bekaert,[175] and Bonfiglioli and Medicino,[176]), while others view it as negative (Eichengreen and Leblang, 2003). Alessandra Bonfiglioli[177] in her study found the following result reflected in the financial liberalization: (1) The effect of financial liberalization on TFP (Total Factor Productivity) is positive and large in magnitude, while it is weak and non-robust on investments, (2) The impact on TFP is both on levels and growth rates, implying that financial liberalization is able to spur GDP growth in the short as well as in the long run, (3) Financial liberalization raises

---

[168] *Ibid.*

[169] Hossein Askari, Zamir Iqbal and Abbas Mirakhor, *Globalization & Islamic Finance: Convergence, Prospects & Challenges*, 177.

[170] Alessandra Bonfiglioli, "How Does Financial Liberalization affect Economic Growth?," (Seminar Paper No.736, Institute for International Economic Studies, Stockholm University, Sweden, 2005), 2.

[171] Grilli, Vittario and Gian Maria Milesi-Feretti, "Economic Effect and Structural Determinants of Capital Controls," (IMF Staff Papers, Vol. 42, No.3., 1995).

[172] Kraay, Aart, "In Search of the Macroeconomic Effects of Capital Account Liberalization," (Working Paper of The World Bank Group, 1998).

[173] Rodrick, Dani, "Who Needs Capital-Account Convertibility?" (Contribution paper to a symposium edited by Peter Kenen, to be published as part of a Princeton Essay in International Finance Harvard University, Mimeo, 1998).

[174] Levine, Ross, "International Financial Liberalization and Economic Growth," (Review of International Economics 9, 2001), 688-702.

[175] Bekaert, Geert, Campbell R. Harvey and Christian Lundblad , "Does Financial Liberalization Spur Growth?" *Journal of Financial Economics,* (Vol. 77, no. 1 (July 2005)): 3-55.

[176] Bonfiglioli, Alessandra and Caterina Mendicino, "Financial Liberalization, Banking Crises and Growth:
Assessing the Links," (SSE/EFI Working Paper (No.567), 2004).

[177] Alessandra Bonfiglioli, "How Does Financial Liberalization affect Economic Growth?," 4.

only the probability of minor banking crises in developed countries, (4) Banking crises harm both capital accumulation and productivity, (5) Institutional and economic development amplifies the positive effects of financial liberalization on productivity and limits the damages from banking crises, and (6) Neither financial liberalization nor banking crises affect the speed of convergence in TFP growth rates. Alessandra then concluded that literatures on the effect of financial liberalization on GDP growth often find mixed results. In order to better understand the effect, it is important to know the channels through which it operates.[178]

Reinhart and Kaminsky[179] have another view on financial liberalization. By providing a sample from 25 countries as evidence, both researchers concluded that financial liberalization has a predictive power on banking crises. In other study, Kaminsky and Schmukler[180] found that the financial liberalization negative effect happened in three to four years immediately after liberalization and then the positive growth effects tend to emerge.

According to Mervyn, one manifestation of globalization is an intensification of international trade and an increase in the scope and significance of all kinds of cross-border transactions. A second feature is an expansion of foreign production via foreign direct investment and the development by corporations of international production and distribution strategies.[181]

From the above studies, it could be concluded that the globalization having a great relation to economic and capital objective. The impact of the globalization is somehow different as viewed by the scholars where their differences are reflects to their experience and observation.

---

[178] *Ibid.*,7.

[179] Kaminsky, Graciela and Sergio Schmukler, "The Twin Crises: Causes of Banking and Balance-of-Payments Problems," (American Economic Review, 89 (3), 1999), 473-500.

[180] Graciela Laura Kaminsky and Sergio Schmukler, "*Short-run Pain, Long-Run Gain: The Effects of Financial Liberalization*," (United Kingdom: Oxford University Press, 2008).

[181] Mervyn K. Lewis, *The Globalization of Financial Services,* xiii.

3.2. THE FEATURES OF FINANCIAL LIBERALIZATION

The feature of financial liberalization comprises certain main elements, namely multinational banking, offshore financial center and international financial centre. This topic will discuss in brief each of the process of financial liberalization and towards the establishment of financial centres:

1. Multinational Banking
2. Offshore Financial Center
3. International Financial Center
4. Global Financial Centre

3.2.1 Multinational Banking

Multinational banking as defined by Grubel[182] is "the ownership of banking facilities in one country by citizens of another." Jones[183] defines as "a multinational bank owns and control branches and/or affiliates in more than one country." Buckley and Casson[184] in their study stated, "in line with the economic theory of multinational enterprises, this definition highlights that multinationalization differs from internationalization inasmuch the former implies both foreign direct investment and the control of foreign units." Instead, many contemporary studies used the term "foreign banking." The use of the description "multinational" in a banking sector seems more appropriate in signifying the banks, which operate in the immense number of countries and wide geographic regions. Lewis and Davis provided the evidence of this point.[185]

---

[182] Herbett G.Grubel et.al., *The Globalization of Financial Services: An Overview*, (Cheltenham: United Kingdom, Edward Elgar Publishing Limited, 1999), xvii.
[183] Geoffrey Jones, *Banks as Multinationals*, (London: Routledge Publication, 1992), 1-13.
[184] Buckley, P.J. and M. Casson, *The future of the Multinational Enterprise*, (London: McMillan, 1991).
[185] M.K. Lewis and K.T Davis, *Multipliers and the Portfolio Approach: A Geometric Exposition*, (Appendix to Domestic and International Banking, Philip Allan Publishers Ltd., 1987), 310 – 313.

However, Mervyn in his comment on Grubel's view on multinational addressed that multinational might be defined in terms of share of ownership (e.g. a company owned by a citizen of many countries), with the attention more upon corporate governance rather than the pattern of production and distribution.[186]

According to Grubel, the benefits of multinational banking appear in three forms: First, countries which permitted the business of retail banking by foreign banks, the multinationals causes an actual or potential competition, reducing the power, potential and wastes of the typical national banking oligopolies. Second, the multinational banks provide valuable services using its knowledge capital at a very low marginal cost; a similar way to the multinational manufacturing enterprises. Third, the multinational banks spur the efficiency of capital flows, especially through the speed of capital moves and the customers' level of capabilities.[187]

Calzolari and Loranth stated that the advantages of multinational banks derived from operating efficiency and production complementarities consists of various factors such: superior accumulated management skills, international reputation, knowledge and experience, entrepreneurial resources as management technology, organizational and marketing know-how and commercial intelligence. All these advantages show a public good implemented within the firm, which can be best exercised in other foreign countries.

Multinational banking also has a cost to be borne as highlighted by Grubel, which took three basic forms: First, there will be a discriminatory treatment from the government regulations toward multinational banks and other banks, which aims to eliminate certain perceived externalities. Second, a special type of externalities becomes a matter, which national banking systems attempt to eliminate through compulsory minimum reserve requirements and control over the reserve base. All these reactions are

[186] Mervin K. Lewis, *The Globalization of Financial Services*, xvii.
[187] Herbett G.Grubel et.al., *The Globalization of Financial Services: An Overview*, 114.

caused by the cyclical fluctuations in the money supply, income, employment, prices and the balance of payments. Third, some factors of inflation crisis are apparently caused by multinational banks through the increasing liquidity of the deposits' multiple expansions in the Euro-dollar market. In addition, the increase of efficient use of existing capital has caused the global velocity of money and created inflationary pressure in all countries.[188] Bain[189] stressed that the next step for the internationalization is a shift from multinationalization to global banking. The latter implies much more coordination among the bank's activities all over the world.

Hence, the expansion of local banking institutions so called multinational banks across borders is among the important feature of financial liberalization. The expansion of domestic banking institutions benefits the institution in term of competency and capabilities to sustain within the international business climate which absolutely tougher than internal challenges. The expansion means more business could be created and the increase of customers will benefit the home shareholders.

The existence of multinational banking institutions portrayed the comprehensive facilities available in a country consist of the advance of technology development, the availability of infrastructure, speed and fast system in many areas such telecommunication, IT system, transportation and many others.

3.2.2 Offshore Financial Centers

The Offshore Financial Centers of OFC could be considered as one major element in the formation of financial center. Historically, the "offshore" system of the international banking sector eminently started in the 1960s and 1970s and becomes a new character of banking business transacted in a location outside a country in whose currency business is denominated. Thus, the "offshore" banking system is often called

---

188 Herbett G.Grubel et.al., *The Globalization of Financial Services: An Overview*, 114.

189 Elisa Bain, Justin G. Fung and Ian R. Harper, "Multinational Banking: Historical, Empirical and Case Perspectives," (Melbourne Business School Working Paper, N.5,1999)

the "eurocurrency" market. For instance, Eurodollar transactions are conducted outside the United States and eurosterling transactions are conducted outside Britain. Much of this offshore business occurs in major financial centers like London, although some business is literally in the islands offshore the United States such as the Bahamas or Cayman Islands.[190]

Literally, Hampton defines OFC as "*a centre that hosts financial activities that are separated from major regulating units (states) by geography and or by legislation. This may be a physical separation as in island territory or within a city such as London or the New York International Banking Facilities (IBFs*)."[191]

According to Rossidue-Papakyriacou,[192] "*An offshore center is a country, which offers to the residents of other countries the ability to establish companies and to use its financial services for activities outside this center, offering in most of the cases some advantages such as low taxation rates. In other words, the aim of the users of the offshore centers is to take advantage of the lower tax rates offered by the offshores centre, which is not synonymous to tax evasion as is the general perception. Certain jurisdictions establish themselves as offshore financial centres in order to attract funds, provide jobs and facilitate economic development*."

Tax havens and Offshore Financial Centres (OFCs) have an important function in the circulation of international financial capital, acting to observe the global financial centers of London, New York and Tokyo. The OFC roles can be described as a place where actual financial activities operate in the place, with the presence of many banks

[190] K. Alec Crystal *et.al* , *The Globalization of Financial Services: An Overview*, (Cheltenham, United Kingdom: Edward Elgar Publishing Limited, 1999), 327.

[191] Mark. P. Hampton, "Treasure Islands or Fool's Gold: Can and Should small Island Economies copy Jersey," *Journal of World Development*, (Vol. 22, No.2, Elsevier Ltd., 1994), 237.

[192] Rossidou-Papakyriacou E , "Internatioanal Co-Operation in the Fight against Corruption from the point of view of an Off-shore Centre," (paper presented at the 4th European Conference of Specialised Services in the Fight against Corruption, Limassol (Cyprus), 20-22 October, 1999).

as well as other financial services such as fund managers, trust companies, etc.[193] International monetary fund[194] had underlined four major function of OFC as follows:

1. Offshore banking, which is able to manage foreign exchange operations for corporations or banks. These operations are not subject to other matters such as capital, corporate, capital gains, dividend or interest taxes or to exchange controls;
2. International Business Corporations (IBCs), which enjoy tax-exempt, limited-liability companies used to operate business or raise capital via issuing shares, bonds, or other instruments;
3. Offshore insurance companies are established by their headquarters in order to minimize taxes and manage risk. It is also aimed to reinsure certain risks and reduce their reserve and capital requirements;
4. Offshore regulation on asset management and protection gives an advantage to individuals and corporations to keep their assets in security, in situation where a political and domestic banking systems collapse and unstable. Offshore centre also provides protection to individuals who face unlimited liability at home, which may protect his assets from domestic lawsuits.

One key factor prompted the growth of offshore financial centres are the needs and demands of multinational business. The spread and rise of business, which becomes more internationalized, requested for diverse international financial services. It has become a suitable place, where companies from various countries seek funding sources in different currencies as an outlet to place temporarily idle fund's access to different types of credit facilities and for the purpose of money transfer across international

[193] Mark P. Hampton et. al, *The Globalization of Financial Services: An Overview*, (Cheltenham, United Kingdom: Edward Elgar Publishing Limited, 1999), 417.
[194] International Monetary Fund, “Caribbean Centers, Stricter Rules Change Climate for Offshore Financial Centers,” (in IMF Survey, vol.31, n.15, August, 2002), 252-253.

barriers. Tax laws and foreign exchange restrictions become crucial factors in influencing transaction of international business. Thus, OFC benefits multinational companies to execute international financial transactions, which are free from most tax consequences and foreign exchange controls. It gives more efficient and quick service in fulfilling customer's need in depositing their money in offshore.[195]

According to Ian McCartney,[196] the most important thing for countries to establish offshore centers is the consideration of the costs and benefits. Among the objectives of a country's decision to specialize in the offshore business are to make requisite amendments to legislation, to invest in telecommunications and infrastructures, to accept the potential indirect costs - each of these is depending on an explicit assessment of the expected future net welfare gain, discounted overtime.

Currently, there are some movements for a new type of financial centre, namely Global Finance Centre (GFC) such as the cities of London, New York and Tokyo. Therefore, there is presently an appearance of a regional grouping of three economic blocs, namely the EU, North America and Asia Pacific.[197] The objective behind the establishment of OFC to GFC is somewhat different in the Asia-Pacific area, where the financial activity in Tokyo is different compared to New York and London. Hong Kong and Singapore are considered as a regional centre than normal OFCs.[198] The city of London is an example of an operational offshore financial centre. On the other hand, the Bahamas and the Cayman islands emerge as the place of booking centres.[199]

3.2.3 International Financial Centres

---

[195] Henry C. Wallich et al., *The Globalization of Financial Services: An Overview*, 316.
[196] Ian Mc Cartney et.al., *The Globalization of Financial Services: An Overview*, (Cheltenham: United Kingdom, Edward Elgar Publishing Limited, 1999), 324.
[197] Mark. P. Hampton, *The Globalization of Financial Services: An Overview*, 422.
[198] *Ibid.*
[199] Henry C. Wallich et.al., *The Globalization of Financial Services: An Overview*, (Cheltenham, United Kingdom: Edward Elgar Publishing Limited, 1999), 315.

A "financial center" is a city that concerted financial and economic activities such as banking, insurance and ancillary types of financial business – where this centre caters to a region outside the city itself, which may include other cities as well. An "international financial centre," such as London or New York and in a lesser way Paris, Hamburg and Zurich, function as financial centres to provide financial services within the region and beyond the boundaries of the countries where its aim to embrace the whole world or substantial part of it.[200] Centres are by definition cities, which become the center of businesses, which are not necessarily involved in an international business. The majority of International financial centres such as London, New York, Zurich and Singapore are domestic-based business, which does not involve international or interregional trade. All countries have an international trade in financial services, but only a small number has international financial centres.[201]

According to Yousef Cassis, [202] based on the historical study, to date, the most significant conditions in the development of international financial centres could be summarized as follows:

- Stability of political institutions;
- Strength of the currency;
- Sufficient savings that can readily be invested abroad;
- Powerful financial intermediation;
- Firm but not intrusive state supervision;
- Light tax burden;
- Highly skilled workforce;
- Efficient means of communication; and
- Plentiful, reliable and widely accessible information.

[200] *Ibid.*, 334.
[201] H.W Arndt, *The Globalization of Financial Services: An Overview*, (Cheltenham, United Kingdom: Edward Elgar Publishing Limited , 1999), 24.
[202] Y. Casis, *Capitals of Capital: A History of International Financial Centres*, *1780-2005* (United Kingdom: Cambridge University Press, 2006), 279.

The above list of features can be considered as the most relevant features to those who seek guidance to develop specific financial centres[203].

Current evaluation on financial centers conducted by Z/Yen company shows the ranking of financial centres around the world as displayed in the following table:

Table 3.1: GFCI 17 Financial Centre Profiles

	Broad and Deep	Relatively Broad	Relatively Deep	Emerging
Global	**Global Leaders**	**Global Diversified**	**Global Specialists**	**Global Contenders**
	Frankfurt	Amsterdam	Beijing	Moscow
	Hong Kong	Brussels	Dubai	
	London	Dublin	Geneva	
	New York	Paris	Luxembourg	
	Seoul			
	Singapore			
	Tokyo			
	Toronto			
	Zurich			
Transnational	**Established Transnational**	**Transnational Diversified**	**Transnational Specialists**	**Transnational Contenders**
	Boston	Copenhagen	Abu Dhabi	Bahrain
	Busan	Doha	British Virgin Islands	Bahrain
	Chicago	Istanbul	Casablanca	Edinburgh
	Montreal	Kuala Lumpur	Shenzhen	Gibraltar
	Shanghai	Madrid		Jakarta
	Sydney	Milan		Jersey
	Washington DC	Prague		
Local	**Established Players**	**Local Diversified**	**Local Specialists**	**Evolving Centres**
	Johannesburg	Athens	Calgary	Almaty
	Melbourne	Bangkok	Dallan	Bahamas
	Munich	Budapest	Riyadh	Bermuda
	Osaka	Lisbon	Taipei	Cyprus
	San Francisco	Mexico City		Glasgow
	Stockholm	Oslo		Guernsey
	Tel Aviv	Rome		Helsinki
	Vancouver	Sao Paolo		Isle of Man
	Vienna	Warsaw		Malta
				Manila
				Mauritius
				Monaco
				Mumbai
				Panama

[203] Douglas W.Arner, "The Competition of International Financial Centres and the Role of Law", (University of Hong Kong, Research Grant HKU 7401/05H, 2007), 196.

				Reykjavik
				Rio De Janeiro
				St. Petersburg
				Tallinn

Source: The Global Financial Center Index 17 (March 2015).

David Reim and Charles Calomiris view that the minimum feature of financial centre could be described as; financial system typically comprises simple currency, simple payment, simple banking and simple insurance activities. Both suggested that:

"*The most primitive function of a financial system is to issue and safeguard money. The next function to evolve is a payment mechanism, typically a check-clearance system, which enables parties to transfer money among each other without taking the risk of delivering it in coin or currency. These basic functions are the domain of banks, which are invariably the first financial institutions to evolve in a developing country.*"

According to Beim and Colomiris,[204] a financial system in a fully developed and competitive economy comprises a comprehensive financial institution of banks, specialized financial intermediaries such as finance companies and mortgage brokers, securities firms as well as institutional investors such as insurance companies, pension funds and mutual funds. Such financial system plays an important role in mobilizing private saving and investment. It creates various types of saving and investment options for individuals – some at higher risk, some at lower risk, some for a long term and some for a shorter term.

Samuel Huntington suggested that beyond economic and financial significance, the increasingly world economy and politic will organize along civilizational lines, with major civilizations forming economic and political groupings (e.g., Western Islamic, Japanese, Chinese, Indian).[205] In some aspects, the financial centres will develop in the sense of cultural commonality, as has been the case with London and New York for

[204] D. Beim & C. Calomiris, *Emerging Financial Markets*, (London: McGraw Hill, 2001), 44.
[205] Samuel P. Huntington, *The clash of Civilizations and the Remarking of World Order*, (London: Touchston Book, 1998).

Europe and North America. The significant international financial centres such as Southeast Asia and the Middle East would rise with both cultural and economic aspects. This division is related to time zones where financial centres are often targeted, with a general focus on the America, Europe, the Middle East and East Asia. This is already taking place and remains an area of competition, especially in the East Asia and the Middle East.[206]

3.2.4 The Global Financial Centers

The global financial center is a new term to reflect the most effective financial centre among others. It is more effective than international financial centre. Research on the financial centre conducted by Z/Yen group, in their Global Financial Centres Index 3 (GFCI3)[207] found a difference between the Global Financial Centres and the International Financial Centres. The research result indicates that only two centres that can be claimed to fulfill the role as global financial centres, namely London and New York. Global financial centres could be identified as "*a city within, having a sufficient critical mass of financial services institutions to operate with intermediaries and to connect international, national and regional financial service's participants directly*." For example, an asset manager in Munich, can directly trade in financial instruments with a broker in New York without having to use the usual practices via an intermediary in, for example, Frankfurt. An international financial centre is interpreted as "*a centre to conduct a huge number of cross-border transactions involving at least two locations in different jurisdictions*." For instance, in Asia, Hong Kong is an international financial centre that successfully involved in a significant proportion of Asian transactions.[208]

---

[206] Douglas W.Arner, "The Competition of International Financial Centres and the Role of Law," 16.
[207] The Global Financial Centres Index 3(GFCI3) is the third report produced by the Z/Yen Group for the City of London which ranks financial centres based on external benchmarking data and current perception of competitiveness.
[208] Mark Yeandle, Alexander Knapp, Michael Mainelli and Ian Harris, "The Global Financial Centres Index 3, 15.

In the past, a strong domestic economy became a vital factor in developing international financial centres. Yet, this factor, recently found to have no correlation with the rating of financial centres as research conducted by the group as summarized in their first issuance of Global Financial Centre (GFC1). This is evidenced from an observation on the US economy, which is at least five times larger than that of Britain's, but London and New York are rated similarly as financial centres.[209]

In reality, the 'traffic' between the domestic economy and the global financial community is somehow critical. The key function of the domestic financial community is not based on its ability to provide service to domestic economy's needs domestically, but through its ability to service the domestic economy's needs wherever and however they are best serviced. Therefore, the key measure for the financial centre will include its effectiveness in providing services locally and its best service at providing choice and access to global financial services globally. Based on this measure, it is realized that a hindrance for developed financial centre was the protection policy towards domestic financial players. Competition in liberalized economy may lead to a clear link with the global financial markets and connectivity to global finance is crucial to national economic performance.[210]

The rating of global financial centers has been made by London-based Global Financial Centres Index (GFCI). The rating was made by assessing the following key areas:[211]

1. People - Involve the good personnel availability, the labour market flexibility, business education and the development of "human capital."
2. The Business Environment – covers regulation, tax rates, levels of corruption, economic freedom and the ease of doing business. Regulation, a major component of the business environment, is cited by questionnaire to

[209] *Ibid.*, 16.
[210] *Ibid.*
[211] *Ibid.*, 9 – 10.

respondents as a decisive factor in the competitiveness of London and New York. The online questionnaire contains a question about the most important competitive factors for financial centres.

3. Market Access – covers the levels of securitization, volume and value of trading in equities and bonds as well as the clustering effect of having many firms involved in the financial services sector together in one centre.
4. Infrastructure – Has to do mainly with the cost and availability of buildings and office space, although it also includes another infrastructure factor such as transport.
5. General Competitiveness – covers the overall competitiveness of centres in terms of more general economic factors such as price levels, economic sentiment and how centres are perceived as places to live.

The following table shows an example of the top ten financial centers ranked in the Global Financial Center Index:

Table 3.2: The following table shows the Top 10 GFCI's financial centres ratings:

Centre	**GFCI 17**		**GFCI 16**		**Changes**	
	Rank	Rating	Rank	Rating	Rank	Rating
New York	1	785	1	778	-	+ 7
London	2	784	2	777	-	+ 7
Hong Kong	3	758	3	756	-	+ 2
Singapore	4	754	4	746	-	+ 8
Tokyo	5	722	6	718	+ 1	+ 4
Zurich	6	719	7	717	+ 1	+ 2
Seoul	7	718	8	715	+ 1	+ 3
San Francisco	8	708	5	719	- 3	-11
Chicago	9	707	12	702	+ 3	+ 5
Boston	10	706	9	705	-1	+ 1

Source: The Global Financial Center Index (2015).

With regard to Muslim countries, their financial center were rated in the seventeenth GFCI ranking in 2015 which among of them headed by Riyadh was ranked at 14th , Doha at 20th, Dubai at 23rd, Abu Dhabi at 26th , Kuala Lumpur at 38th , Istanbul at 44th , Bahrain at 46th and Jakarta at 57th.

Table 3.3: Islamic Financial Center ranking in GFCI 17:

Centre	GFCI 17		GFCI 16		Changes	
	Rank	Rating	Rank	Rating	Rank	Rating
Riyadh	14	698	21	685	+ 7	+13
Doha	20	691	22	684	+2	+7
Dubai	23	688	17	694	-6	-6
Abu Dhabi	26	685	19	692	-7	-7
Kuala Lumpur	38	652	41	656	+ 3	-4
Istanbul	44	643	42	655	-2	-12
Bahrain	46	641	52	634	+ 6	+ 7
Jakarta	57	618	66	620	+ 9	-2

Source: The Global Financial Center Index (2015).

This study found that the research conducted by Z/Yen group has successfully defines the global financial center in a clear meaning and view. The group also provides a clear feature of global financial center and it difference to another level of financial centers namely international, regional and national.

3.3. MALAYSIA'S DOMESTIC FINANCIAL REFORMS

The globalization movement will go ahead towards the greater liberalization of the financial system; this process will be through the reducing of barrier to entry in the domestic financial sector, which could intensify competition over time. Thus, it is important for the financial institutions to be able to manage the international capital flows, particularly the short-term capital flow. Something that can be learnt from the Asian crisis is the reversal of short-term capital flow, which caused problems to the management of the macroeconomic policy. Malaysia is a small open economy where the international capital flows beyond what the domestic financial market could support such kind of flows resulted in sharp movements in interest rates, exchange rates and asset's prices.[212]

Therefore, in the 1980s and 1990s, the domestic financial market's liberalization

[212] *Ibid.*

consisted of internal liberalization through mergers and acquisitions. Restriction was imposed for both domestic and foreign firms where they are not allowed to open branches or to operate ATMs. In addition, there was a limitation for foreign participation in domestic banks whereby the shares are limited to 30 percent ownership and in other financial firms, up to 49 percent ownership. Hence, Malaysia's domestic financial liberalization does not directly lead to overshooting and macro-economic instability. During the economic crises held in 1997, however, the blame was thrown partly to the capital account liberalization for the macro-economic instability experienced during the period.[213]

In describing Malaysia's experience from the aspect of financial liberalization effects, Mustapa Mohamed[214] said many countries benefit from globalization by removing remaining restrictions. Malaysia also tempted to remove remaining restrictions, especially in the capital flows. Nonetheless, the government took a stand to retain control on the private sector's capital flows and the control on the private sector itself. This situation became a critical factor in separating Malaysia from other countries in the region. Although affected by the regional crisis, Malaysia has been fortunate enough to be spared of worse consequences, partly due to Malaysia's relatively low foreign currency borrowing.[215] Mustapa added, Malaysia's economic strength prior to the crisis was not mainly due to globalization. While globalization could become a contributing factor, the identified factor for the success of Malaysia was its fundamental strength. The government also plays a major role in setting up the sound policies together with the capacity of the Government to administer the country well.[216]

---

[213] *Ibid.*
[214] The adviser to the Minister of Finance, Malaysia (2000 – 2001).
[215] Mustapa Mohamed et.al., "Globalization: A Malaysian View," in Nik Mustapha Nik Hassan, *et al. (ed), The Economic and Financial Imperatives of Globalization: An Islamic Response,* (Kuala Lumpur: IKIM, 2000), 4.
[216] *Ibid.*

3.4. MALAYSIA ISLAMIC FINANCE GLOBAL HUB VISION

Malaysia is constantly undertaking efforts to promote the country as a regional Islamic financial centre. For this purpose, Labuan has been set up as an International Offshore Financial Centre (IOFC) inclusive of Islamic banking and capital markets. In the strategic plan, the aim is to expand the offshore financial service's opportunities from Asia-Pacific and other established IOFCs. Measures and initiatives are being undertaken to equip Labuan IOFC with the appropriate infrastructure, institutional capacity as well as legal aspects to position Labuan as an efficient and highly rated Islamic financial center in the region.

The internationalization of Malaysia's Islamic finance is encapsulated in the Malaysia International Financial Centre (MIFC) initiative. This project involves several parties of the community inclusive of international and domestic participants offering *Sharī'ah* compliant products and services; Government ministries and agencies as well as regulatory authorities are working collaboratively in the field of Islamic finance. The Islamic finance in Malaysia has been developed since 30 years ago. Thus, Malaysia is well equipped with experience of talents and personnel in Islamic finance. This expert includes various fields of Islamic finance and inclusive of the global jurisdictions. In addition, Malaysia welcomes new players to establish operations in the country.[217]The internationalization of Islamic finance in Malaysia comprises four main sectors of Islamic finance, namely Islamic Banking, Islamic Capital Market, Islamic Fund Management and *Takaful* and Re-*takaful*.

[217] Malaysia International Islamic Financial Centre, "*The MIFC Community Directory: Connecting Business with Islamic Finance*, vol.2, (Kuala Lumpur: Malaysia International Islamic Financial Centre, 2010).

The evolution of Islamic finance in Malaysia is highlighted in the speech of the Governor of Central Bank of Malaysia, Dr. Zeti Akhtar Aziz:[218]

"*In the initial stage during the early years of the development of the Islamic financial system, the focus of attention was on the development of the Islamic banking system and to expand the number of players and the volume of banking activity. This expanded significantly when the dual banking system was introduced and was subsequently extended to the specialized non-bank institutions, including the development financial institutions, where Islamic financial products and services are being offered. The other core components of the Islamic financial system comprised the Islamic money market, the Islamic capital market and the takaful market*." The story of Malaysia's Islamic finance evolution could be categorized into three sectors, namely Islamic banking, Islamic Capital Market and *Takaful*. The following studies show the path of Malaysian Islamic finance liberalization.

3.4.1 Malaysia's Islamic Banking Liberalization

In an Islamic banking sector, a global benchmark has been set in Malaysia's Islamic banking with its critical mass of players and innovative competitive products. Malaysia also has a number of innovators and thought leaders in Islamic banking. The innovation work has been intensified over the years, which includes the development of the sophisticated Islamic financial instruments such as structured based to cater the demand in the market. As a result, Malaysia enjoys a wide range of Islamic financial

[218] Zeti Akhtar Aziz, "Islamic Finance – Dynamic Industry in a Rapidly Changing Global Environment," (Governor's Keynote Address at the 2nd International Islamic Finance Conference at Crowne Plaza Hotel, Dubai, U.A.E, 22 September 2003), pp.71.

instruments. A major strength behind Malaysia's Islamic banking industry is its access to the active, deep, liquid and Islamic money market. This provides the platform for funding activities. The industry is also equipped with a variety of hedging tools such as currency swaps and Islamic forward contracts. Due to these facilities, it enables financial institutions to reflect the Islamic principles in both substance and form as end-to-end banking transactions can comply with *Sharī'ah*. In addition, the issuance of the world's first electronic multicurrency commodity trading platform, Bursa *Suq al-Sila*' facilitates financing for Islamic financial institutions and liquidity management. Bursa *Suq al-Sila*', which is operated by Bursa Malaysia, functions to facilitate cross-border intermediation between institutions across multiple markets.[219]

In the section of global corporate banking, there is *Sharī'ah* compliant version of product portfolio, consists of investment and underwriting services, asset and commodity finance, commercial insurance, brokerage's services and foreign exchange products, which merit further development. For the global investor segment, the product portfolio should include *Sharī'ah* compliant tax efficient investment accounts, unit investment trusts, personal pension, retirement planning, mutual funds, closed-end funds and medium net worth wealth management service. The merge of all these products are as a result of join collaboration effort between the Islamic scholars and the practitioners.[220]

The future path for Islamic investment and financial institutions is to have continuous changes and improvement. The improvement of Islamic financial infrastructure must constantly work progressively to cater the complex and different demands from various economy sectors and society in the current globalized and

---

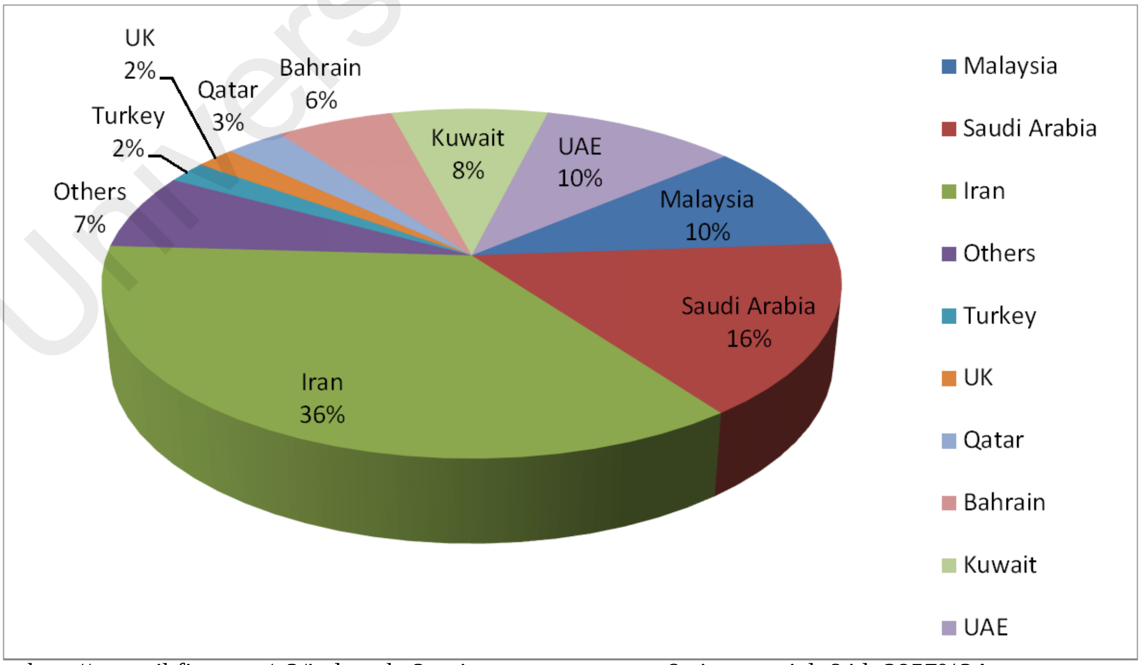
[219] Malaysia International Islamic Financial Centre, "*The MIFC Community Directory: Connecting Business with Islamic Finance*, vol.2,

[220] Y.M. Raja Dato' Zaharaton Binti Raja Zainal Abidin, "Globalisation: Prospects for Islamic Investment and Financing,"(Paper Presentation by the Director General, Economic Planning Unit, Prime Minister's Department), 6.

liberalized world. In particular, the new and emerging opportunities for investments in this era of globalization can be tapped if Islamic Investment funds, among others, establish global consortiums to finance multi-national projects.[221]

In the meantime, the Central Bank of Malaysia has announced to issue up to two licenses of Mega Islamic Bank as stated in the statement by the Central Bank of Malaysia's Governor on 27 October 2010: "We will announce one mega Islamic bank," the Governor Tan Sri Dr Zeti Akhtar Aziz said on the sidelines of the Global Islamic Finance Forum 2010.[222] However, until this study was conducted, there is yet an Islamic Mega Bank in Malaysia. Due to the large capital needed, which is at least US$1 billion (RM3 billion) for the establishment, the announcement has been delayed several times.[223] Up to date, there are 17 Islamic banks in Malaysia; 11 are local and the rest are units of big lenders like Standard Chartered, HSBC Holdings and Kuwait Finance House.[224] The following chart shows Global Islamic Banking assets in 2009.

Chart 3.1: Islamic Banking and Finance Shares, 2009.



http://www.ibfim.com/v2/index.php?option=com_ content&view= article&id=2957%3Aone-mega-islamic-bank-this-year&Itemid=179.

[223] Business Times, "Where is Malaysia's Mega Islamic Bank?, retrieved on 7 December 2011, http://www.btimes.com.my/Current_ News/BTIMES/articles/Babyx/Article/index_html.

[224] *Ibid.*

Sources: The Banker Top 500 Islamic Institutions, November 2009.
(From Gateway to Asia: Malaysia. International Islamic Finance Hub Publication).

3.4.2 Malaysia's Islamic Capital Market Liberalization

The Malaysia's Islamic capital market witnessed a significant development in product innovation and financial intermediation, especially in the Islamic equity sector and fixed income sector. Malaysia became the largest issuer of *sukuk* among global countries, representing 65% of the global outstanding *sukuk* by June 2010; a total value exceeding USD 89 billion.[225] Malaysia is also equipped with the biggest Islamic equity market and residence to become four of the top 10 largest *Sharī'ah*-compliant companies in the world.[226] The Securities Commission of Malaysia classifies more than 85% of the stocks listed on Bursa Malaysia, the national exchange that complies with *Sharī'ah*. Besides size, the Malaysia's Islamic capital market also leads in product innovation and sophistication. In order to fulfill the market demand for diversification strategies, the expert gives the best effort in structuring innovative, investable products such as the world's first Islamic real estate investment trust (I-REIT) and Asia's first Islamic exchange-traded fund (I-ETF).[227]

In addition, the spurring factor of government incentives and rapid liberalization of the Islamic financial industry in Malaysia has resulted in a dynamic and diverse community of foreign and domestic fund management. Thus, the presence of these Islamic fund management companies can steer for the quick building of a *Sharī'ah*-

---

[225] Bank Negara Malaysia, *MIFC: Malaysia: Your Business Connection To Global Islamic Finance,* (Kuala Lumpur, Malaysia: Bank Negara Malaysia, 2010), 40.
[226] PricewaterhouseCoopers, *Gateway to Asia; Malaysia, International Islamic Finance Hub,* (Kuala Lumpur: PricewaterhouseCoopers, 2010), 56.
[227] *Ibid.*

compliant investment in Malaysian multinational corporations with the regional reach around Asia. In the meantime, the companies can also become the country's centralized location to seek *Sharī'ah*-compliant investing opportunities within the region. Recent innovations of the Malaysian Islamic fund management include pioneering Islamic funds that give exposure to India, Indonesia, Taiwan, Australia and Korea as well as the highly lucrative market in China. The Malaysia's vibrant Islamic fund management industry offers many benefits to the investors. Among others, it provides opportunities of using the industry's expertise and capabilities in identifying *Sharī'ah*-compliant investing opportunities across Asia, to leverage on the enabling environment for Islamic finance and pro-business policies and procedures for Islamic fund management. Cross-border marketing and distribution of Islamic funds came into existence by the mutual recognition agreements signed between Malaysia and other jurisdictions.[228]

The Prime Minister of Malaysia, in his speech at Invest Malaysia on 30 June 2009 announced that there would be further liberalization to various segments of the capital market. The liberalization will initiate to further enhance the Malaysian capital market's attractiveness and promote greater competition and provide a broader choice of intermediation services.[229] These efforts include the liberalization of the equity holdings' requirements of capital market intermediaries, which are licensed in accordance with S58 of the Capital Markets and Services Act 2007 with respect to the following activities:[230]

- Dealing in securities - stock brokers who are not investment bankers;

[228] Securities Commission Malaysia has signed two such mutual recognition agreements; with the securities
and Futures Commission of Hong Kong and with Dubai Financial Services Authority.
[229] Securities Commission Malaysia "Liberalization of Equity Holdings in Capital Market Intermediaries,"
retrieved on 8 December 2011, http://www.sc.com.my/main.asp?pageid=754&menuid= &newsid=& linkid=&type=.
[230] *Ibid.*

- Dealing in securities restricted to unit trust - unit trust management companies; and
- Fund management.

Subsequently, during the Budget 2010 announcement on 23 October 2009, the Prime Minister announced the liberalization of equity requirement of capital market intermediaries with respect to the following activities:[231]

- Advising on Corporate Finance, and
- Financial Planning

3.4.3 Malaysia's *Takaful* Liberalization

In the *Takaful* sector, Malaysia is known with its sophisticated range of products. Malaysia also hosted the global *Takaful* Group, which functions as a platform to enhance business networking among global *takaful* and re-*takaful* players. Collaborating with Malaysia's *Takaful* industry provides many advantages. This range includes the chances to learn directly from industry leaders and to leverage on the enabling environment that has been established for Islamic finance in the country. The formation of innovated *takaful* and re-*takaful* products in Malaysia favours facing different risk profiles; obtain operation efficiencies in a *Sharī'ah*-compliant manner and execute a multichannel distribution of agents (via an agency), brokers, bancatakaful and direct marketing.[232]

Due to the existence of many Islamic finance institutions, Malaysia is keen on developing the country as a global hub for Islamic finance. As in 2011, Malaysia have 17 Islamic banks in which 6 of the banks are foreign-owned with 4 of them are international banks, namely Al Rajhi Banking & Investment Corporation, Deutsche

---

[231] *Ibid.*

[232] Malaysia International Islamic Financial centre, "*The MIFC Community Directory: Connecting Business with Islamic Finance*, 54.

Bank, Bank Syariah Muamalat Indonesia and Unicorn International Islamic Bank Malaysia Berhad.[233] The number of Takaful players are 11 with 3 companies being foreign-owned and one company has an international status.[234]

3.5. MALAYSIA TO BECOME AS A GLOBAL HUB FOR ISLAMIC FINANCE

As Islamic finance/banking industry is growing at the rate of 12-15 percent per annum, cities like Kuala Lumpur, Dubai, Bahrain and London are vying to become the center of the industry, which currently boasts some $1 trillion in assets. At the moment, Dubai holds the title of an Islamic banking hub - but it could soon lose ground, both to traditional competitors like Bahrain, Kuala Lumpur or London or a newcomer on the scene like Singapore.[235]

Malaysia performed well in Islamic finance industry and has built a global reputation since the sector first emerged in 1981. Today, the country is looking to become a global center of excellence by ensuring the following continues:[236]

- From top to down; 'business friendly' government policies to entice regional or global financial institutions/asset management companies to set up more of their Islamic outfits in Malaysia.
- Sustainable policies in the areas of human capital development in the Islamic asset management industry. By this, it covers both those who specialized in Islamic jurisprudence as well as industry practitioners.
- Continuous multi-lateral arrangements on transfer of knowledge and expertise to the Organization of the Islamic Conference (OIC) countries

[233] Bank Negara Malaysia, "List of licensed Banking institutions in Malaysia," retrieved on 18 November 2011, from http://www.bnm.gov.my/index.php?ch=13&cat=banking&type=MB&fund=0&cu=0,
[234] *Ibid.*
[235] Arab News "Kingdom gaining more clout in Islamic Finance," retrieved on 30 Jan 20212, from http://arabnews.com/economy/ islamicfinance/article569065.ece.
[236] Islamic Finance news, *Malaysia: A Global hub for Islamic Finance*, (Issuance: 15th June 2011, Kuala Lumpur: RedMoney, Kuala Lumpur, 2011), 32.

that is keen on developing their respective Islamic asset management industries.

According to the Malaysian Ministry of Finance, in the Economic Report 2011/2012, Malaysia will continue its efforts to strengthen its position as an international Islamic financial centre and contribute towards the internationalization of Islamic finance. The Ministry said that this could be done by developing *Sharī'ah* -compliant products and services as well as tools to facilitate and support cross-border transactions.[237] The ministry quoted as saying that the implementation of the *Sharī'ah* Governance Framework on July 1 2011 would further strengthen the oversight role, authority, accountability, independence and competency of the Board of Directors, the *Sharī'ah* Committee and the Management of Islamic financial institutions on *Sharī'ah* matters.[238]

Malaysia was still the leader in the global *Sukuk* market with 62.7 percent of total global *sukuk* outstanding, as recorded at the end of the first half of 2011, while Bursa Malaysia was named as the top *sukuk* listing destination, with 19 *sukuk* listed, totaling RM88.3 billion, as recorded at the end of July 2011. To ensure sustainable and competitive Islamic banking operations, the Central Bank of Malaysia on April 25 issued a revised guideline on Profit Equalization Reserve.[239] The Islamic finance investment in Asia is keeping growth with *Sharī'ah* compliant investment instruments being offered in local/foreign currencies. The regulators in many countries are freeing up the banks and fund management companies to offer Islamic products. Other non-Islamic countries, such as Hong Kong, Singapore and India, also make a serious effort in offering these alternative instruments. Thailand is also looking at adopting the Islamic finance in their jurisdictions. Investors from Middle Eastern are showing their

---

[237] Bernama, "Malaysia To Enhance Efforts To Become Global Islamic Finance Hub" retrieved on 22 February 2012, http://finance.bernama.com/news.php?id=618391.
[238] *Ibid.*
[239] *Ibid.*

interest in *Sharī'ah*-compliant assets. Thus, there will be a tremendous investment opportunity in Asia in the large, expanding and untapped Muslim population. Malaysia has since allowed the setting up of asset management companies through foreign and local joint ventures. The combination of the best minds in Islamic finance coupled with an international appeal has been a winning formula.[240]

3.5.1 The Meaning of Islamic Finance Global Hub: An Overview

The exact meaning of Islamic finance global hub is yet being identified. The name Islamic finance global hub is reflected from the financial liberalization policy, which provides Islamic financial services at the international level. A global hub is understood as that such service is opened to global players to participate either as a banker or customer in a country as a hub. For further understanding on this issue, the origin of the meaning of financial liberalization must be clearly identified.

Commonly, the word liberalization is synonymous and has interconnection with the word globalization. Globalization can be understood as a process of opening up national economies and markets. It relates to the ease and speed with which knowledge, technology, people, ideas, goods and services and capital interchange from country to country, thus, broadening the extent and form of cross-border transactions and deepening the international character of an economic activity. Sometimes, a differentiation is made between globalization and internationalization, with globalization as the catalyst for change, to which firms respond by becoming more international. As such, globalization is driven by liberalization of trade and deregulation of capital markets, underpinned by technological change, which lowers communication and transport costs and enhances the international tradeability of goods and services.[241]

---

[240] *Ibid.*
[241] Mervyn K. Lewis, "The Globalization of Financial Services: An Overview," in *The Globalization of Financial Services*, ed. William G.Egelhoff, Paul W.Beamish, Joanne E.Oxley and Bernard Yeung, Chris

Whenever the term 'global' is used in the context of financial services, the example regularly cited is the foreign exchange market. It is one of the four "cornerstones" of global financing as identified by Smith and Walter (1992).[242]

The International financial services, according to the Organization for Economic Co-operation and Development (OECD)[243] (1989-1990) definition (of international financial services), comprise of the receipts (exports) from or expenditures (imports) by financial institutions (banks and other credit institutions) in providing or receiving the following services:

i. Income from direct investments received and paid. This item has two sub-categories: a) Undistributed income, and (b) interest.

ii. Income from other (financial) investments received and paid. This item has one sub-category, which is 'interest or dividends received and paid.'

iii. Commissions and/or fees received or paid.

The available data on financial services are divided into three major categories:

i. Financial services provided to or received from non-residents by all the resident financial institutions.

ii. Financial services provided to or received from residents by all the non-resident financial institutions.

iii. The last category relates the above two categories to all inflows and outflows of capital recorded in the corresponding items of the balance of payments.

In recent years, the direct and financial investment income flows have been referred to as factor services and/or factor incomes as they are presumably provided by

---

Milner, James Foreman-Peck, Thomas L. Brewer, John Cantwell, (Cheltenham, United Kingdom: Edward
Elgar Publication, 1999), xiv.

242 *Ibid.*, xxix

243 The Organization for Economic Co-Operation and Development, is an international economic organisation of 34 countries founded in 1961 to stimulate economic progress and world trade. It is a forum of countries committed to democracy and the market economy, providing a platform to compare policy experiences, seek answers to common problems, identify good practices and co-ordinate domestic and international policies of its members.

the capital as a factor of production. However, the OECD (1989 – 1990) has broadened the definition of "international financial services," which formerly covered only those activities related to "commissions and fees," to embrace 'direct investment income flows' and 'foreign financial income flows' for three reasons: (a) the size of the commissions and fees relative to the size of the activities of financial institutions in the area of factor incomes is very small, (b) some of the financial services are embodied in other activities of the financial institutions, for instance, the OECD argues that the bulk of financial services consist of the granting of credit on borrowed funds (an activity measured by factor services); and (c) a number of services are free as they are compensated for by the main activities of the financial institutions.[244] The distinction between total financial investment income flows and the interest attributed to them by the OECD (1989 – 1990) has now offered an opportunity for researchers to know the size of the international financial services charges associated with these financial assets and liabilities. This in turn may capture the amount of international financial services, which as the OECD argued, appear to be free on the face value and/or be part of the major financial activities of institutions (i.e lending activities).[245]

3.5.2 The Meaning of Hub

The term hub is used in this condition to represent the meaning of a central place. The Palgrave Dictionary of Economics[246] defines Central place theory as a collection of loosely related, informal, descriptive models of city size, city location and market area based on the trade-off between increasing returns to scale in production and the cost of transport of goods from firm to home. Land markets are often absent. At its core, the central place theory is an empirically motivated description of production in southern Germany. It is a remarkable empirical motivated description of production in

---

[244] Fariborz Moshirin *et.al*, *The Globalization of Financial Services*, (Cheltenham, United Kingdom: Edward Elgar, 1999), 40.

[245] *Ibid.*

[246] McMillan Publishers Ltd., *The New Palgrave Dictionary of Economics*, ed. 2nd, Vol. 1 , (New York: McMillan Publishers Ltd., 2008), 734-735.

Southern Germany. It is a remarkable empirical regularity in search of a formal theory; a better name would be “central place regularity.” The beginnings of the theory are attributed to Christaller (1933) who first made detailed observations of urban hierarchies and then attempted to model them. The basic ideas put forward are that consumer population is distributed uniformly while firms are located in the cities. Cities form a hierarchy in that cities that are higher in the hierarchy produce all the goods that cities, which are one level lower in the hierarchy produce and one more. The ratio of market areas of a commodity produced only at a given level of the hierarchy (and above) to the market area of a commodity produced at the next lower level of the hierarchy (and above) is assumed to be constant, independent of the level in the hierarchy considered. Thus, the cities in a given area form a hierarchy where the size of a city’s market area and the variety of commodities it offers are perfectly correlated.[247]

3.5.3 The Meaning of Islamic Finance Global Hub

As a conclusion from the above study, it is clearly understood that the financial global hub does not just involve finance but all together with investment and trade.

Thus, the interpretation of Islamic finance Global Hub is proposed as “A country becomes a hub for local and global financial providers in offering Islamic finance services comprises of Islamic banking, Takaful and Islamic financial market for the country’s residents and international customers.”

However, in term of pronunciations, some pronounce as “Global hub for Islamic Finance,” while others refer to it as “Islamic Finance Global Hub.” Regardless of pronunciation, the meaning is referring to the same understanding.

3.6. CHAPTER SUMMARY

[247] *Ibid.*

The presence of Islamic finance around the world is being accepted rapidly in most countries in the Asian, European and American regions. The demand of an alternative financial system is increasing, especially for the best financial system, which is able to ensure a safe, just and non-oppressive system.

Malaysia is keen in promoting the country as an Islamic Finance Global Hub. The process of global hub evolution started from the advancement of domestic financial system and subsequently developed to become as an international hub access. This process includes the expansion of local banking institutions into the international market and the opening of the domestic market to foreign financial institutions.

Given that Malaysia has positioned a clear vision towards the Islamic finance global hub, hence, the country must ensure that all aspects of the Islamic financial system are within an adequate preparation. This may include the advanced systems of Islamic banking, Islamic insurance and Islamic capital market. Further, all supportive aspects of Islamic finance must also conform in the best manner whereby these may include product development, advancement of technology, affectivity and productivity of human talent, the soundness and the flexibility of the government and other Islamic finance support tools to ensure the vision becomes a reality.

CHAPTER FOUR

INITIATIVES OF CENTRAL BANK OF MALAYSIA IN POSITIONING MALAYSIA AS A GLOBAL HUB FOR ISLAMIC FINANCE

4.0 INTRODUCTION

This chapter examines the role undertaken by the Central Bank of Malaysia in positioning Malaysia as the Islamic finance global hub. This study attempts to answer the third question of the problem statement as stated in the first chapter.

Initially, the presence of Islamic banking and finance is significant in the global economic scenario, which presence forms a part of the equation in international finance, either at a government-to-government or the private sector levels. The Islamic banking and finance system is implemented in over 60 countries around the world.[248] In Malaysia, the Islamic economic system emerged since 1963 with the establishment of Tabung Haji, the pilgrims corporation fund. After twenty years, the government of Malaysia established the first Islamic bank, namely Bank Islam in 1983 and followed by the establishment of the first *Takāful* operator, Syarikat *Takāful* Malaysia in 1985. Malaysia's *Sukuk* market commenced in 1990 with a moderate size valued $39 million (RM 125 million) issued by Shell MDS Sdn. Bhd. Two *Sharī'ah* Advisory Councils (SACs) were subsequently set up to provide regulatory guidance on the development of the Islamic finance market, instruments and institutions. These two SACs body are under Securities Commission Malaysia (SC) and Central Bank of Malaysia.[249]

In 2000, CBM and SC had set up a strategic plan including a 10-year period of a development plan, named as Financial Sector Master Plan. In the year 2006, the government had established a special body named as Malaysian International Islamic Finance Centre (MIFC) with the objective to transform Malaysia into an Islamic

---

[248] PricewaterhouseCoopers, "Islamic Finance in Malaysia," retrieved on 1 October 2011, http://www.pwc.com/my/en/issues/islamic-finance-malaysia.jhtml.

[249] Pricewaterhouse Coopers, "*Malaysia, Asia's Islamic Finance Hub*," (Kuala Lumpur, Malaysia: PricewaterhouseCoopers, 2008), 15.

financial hub.[250]The cumulative Government policies, actions and initiatives over the last decade have made Malaysia among the top Islamic finance countries with the largest Islamic finance markets in the world.[251] The industry has achieved a double-digit growth over the last five years. As recorded between 2004 and 2007, the total of outstanding *Sukuk* increased in average 33% p.a. to US$62 billion (RM213 billion), while Islamic banks' total assets grew at 18% p.a. to US$46 billion (RM157 billion) over the same period.[252]

Undoubtedly, one of the biggest challenges of Central Bank of Malaysia as the regulator is to develop a framework for governing, supervising and regulating Islamic banks and *Takāful*. From the Malaysia's regulator's view, the Islamic banks should be under the central bank's control. Thus, Central Bank of Malaysia formed a ten-year Financial Sector Master Plan as well as Capital Market Master Plan to drive the path of Islamic finance in Malaysia. The Masterplan's recommendations aimed to strengthen the corporate governance of banks, encourage strategic alliances among institutions, and promote institutionalized shareholders' activism. This financial strategic plan was designed as a rubric for the direction to position Malaysia as a global hub for Islamic banking and finance.

The main issues to be examined in this chapter can be divided into two major topics. First; the measures taken by Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic Banking and Finance and second, the impact of Malaysia's global hub policy against local Islamic financial institutions. In addition, it is vital to determine the advantages and disadvantages resulted from the Malaysia's global hub policy for the purpose of opportunities and awareness and its effects on the country.

[250] *Ibid.*
[251] *Ibid.*
[252] *Ibid.*

4.1 CENTRAL BANK OF MALAYSIA INITIATIVES IN DEVELOPING ISLAMIC FINANCE SYSTEM IN MALAYSIA

Malaysia's effort in developing Islamic finance in the country consists of three significant stages. The first stage was a period in between 1983-1992 where Malaysia began its Islamic banking system throughout the country. This period witnessed the setting up of Islamic banking and *Takāful* acts together with the permission for the establishment first full-fledged Islamic bank and first full-fledged *Takāful* company.[253]

The second stage was in a period between 1993 – 2000, whereby the building of institutional was in order within this stage. For examples, the establishment of the National *Sharī'ah* Advisory Council and the establishment of the Islamic Interbank Money Market. For the purpose to increase Islamic banking players in the market, the CBM made a decision to amend its legislative side to allow the window-concept of Islamic banking services to be provided by conventional Banks.

The third stage is between 2001- 2010, where the strategic positioning & international integration policy took place. Within this period, there were four objectives of Islamic finance that had been achieved, namely Islamic banking regulatory framework development, the legal and *Sharī'ah* Framework, the products and markets' development and lastly, the enhancement of knowledge and experience. There were also several significant plans launched namely FSMP, the establishment of Islamic Financial Services Board and MIFC. In the years after, the liberalization policy was being implemented to allow foreign players to open their business and subsidiaries in Malaysia. Hence, based on this continuous work, it has resulted in a formation of a successful Malaysia's Islamic finance framework, which positions Malaysia as a leading Islamic banking and finance country among others.

[253] Mohd Razif Abdul Kadir,"Islamic Finance in Malaysia – Evolution & Current Development," (Deputy Governor of Bank Negara Malaysia, Presentation for MIFC Event on October 2009), 2.

4.2 INITIATIVE 1: STRENGTHENING THE REGULATORY POLICY AND SUPPORTING FRAMEWORK

Malaysia's success in developing Islamic finance could be described as unique. This is due to the success of Malaysia in designing an enhanced Islamic finance system to operate parallel with its conventional counterpart. For example, although the Islamic banking system in Malaysia is governed by its own legal framework (Islamic Banking Act 1983), it is also subject to a similar regulatory and supervisory framework as that of the conventional banking.[254] The features of the Malaysian Islamic financial system, namely Islamic banking, *Takāful*, money and capital markets – are considered as highly integrated. These features have been supported by the Malaysian legal and *Sharī'ah* framework, which plays an integral part in developing the Islamic financial sector.

4.2.1 Legal Framework

In a timely connection with the international Islamic finance world, Malaysia is forwarding effort to develop Islamic finance legal framework, which caters for the international requirements.[255] Many countries around the world including France, Japan, Hong Kong, Australia, Ireland, Korea and Lebanon, are interested in Islamic finance and have started to initiate an effort to review their framework to facilitate the introduction of Islamic finance products. This indicates a good sign for a sustainable global growth of Islamic finance to go forward.[256] However, the important thing in Islamic finance jurisdiction development is a legal framework that is conducive and functions to support the operations and growth of the industry.[257] Thus, Malaysia has developed a comprehensive act to govern Islamic banking and finance as follows:

---

[254] Pricewaterhouse Coopers, "*Malaysia, Asia's Islamic Finance Hub*," (Kuala Lumpur, Malaysia: PricewaterhouseCoopers, 2008), 55.
[255] Arab News, "Malaysia Pushing for Islamic Finance Legal Framework," retrieved on 15 October 2011, http://arabnews.com/economy/ islamicfinance/article208977.ece.
[256] *Ibid.*
[257] *Ibid.*

1. The enactment of the Islamic Banking Act 1983 (IBA) and *Takāful* Act 1984 (TA) are the important features of Islamic finance in the regulation and supervision of Islamic banking and *Takāful* companies.[258]
2. The enactment of the Government Funding Act 1983, which is to enable the Malaysian government to issue non-interest bearing certificates for Islamic financial institutions to comply with their instruments and liquidity requirements.[259]
3. The amendment of relevant laws, including the Companies Act 1965, Banking and Financial Institutions Act 1989 and the Capital Market and Services Act 2007, aimed to accommodate the development of the Islamic financial industry.[260]
4. The establishment of dispute resolution platforms for Islamic finance such as the dedicated arbitration rules for Islamic finance under the Kuala Lumpur Regional Centre for Arbitration of Malaysia and a designated judge at the High Court to preside over Islamic finance cases.[261]

The Malaysian legal framework for Islamic finance is known as the most developed and forward-looking in its approach. The Central Bank of Malaysia Act 2009 caters for two different financial systems, namely conventional financial system and the Islamic financial system. However, it is vital to stress that the governing regulatory laws for Islamic finance are separate from those for conventional finance.[262]

In 2010, Malaysian government took initiatives to establish a Law Harmonization Committee with the main objective to review existing Malaysian Islamic finance laws and to propose necessary amendments to give legal recognition to Islamic financial transactions under the law, to provide a facilitative legal framework for the

---

258 Malaysia International Islamic Financial Centre, "Primer to Islamic Finance," (Kuala Lumpur, Malaysia: Bank Negara Malaysia, 2008), 27.
259 *Ibid.*
260 *Ibid*.
261 *Ibid.*, 28.
262 Arab News, "Malaysia Pushing for Islamic Finance Legal Framework," retrieved on 16 October 2011, http://arabnews.com/economy/ islamicfinance/article208977.ece.

Islamic finance industry and develop Malaysian laws as the law of "international facilitative" or in other word the law of choice for international Islamic financial transactions.[263]

The Malaysian parliament also passed a new legislative in the same year that requires all judiciary to refer to and take lead on all *Sharī'ah* matters involved in any court dispute arising from an Islamic financial transaction. This resulted in more confidence in the *Sukuk* market, as for the first time in the world, there is an absolute validity of Islamic financial contracts.[264]

The following table highlights the milestone of the Malaysia's *Sharī'ah* Regulatory environment: [265]

Table 4.1: Milestone of Malaysia's *Sharī'ah* Regulatory Environment

Year	**Subject**
1983	Islamic Banking Act (IBA) 1983 was enacted in Malaysia. The first full-fledged Islamic bank was established in Malaysia.
1984	*Takāful* Act 1984 was enacted to provide regulation for *Takāful* business in Malaysia.
1996	Amendment to Section 124 of Banking and Financial Institution Act (BAFIA) allowing conventional banks in Malaysia to offer Islamic banking products through Islamic windows.
1998	Interest-free Banking Scheme (SPTF) was upgraded to Islamic Banking Scheme allowing conventional banks to open full-fledged Islamic banking subsidiaries.
2001	Malaysia's Financial Sector Masterplan sets target for Islamic Finance to make up 20% of the finance sector by 2010.
2002	Islamic Financial Services Board (IFSB) was established in Malaysia.
2003	Central Bank of Malaysia (BNM) guidelines on Outsourcing of Islamic Banking Operations. (23rd June 2003).
2004	BNM guidelines on Directorship for *Takāful* Operators (8th November 2004).
2005	BNM guidelines on the *Sharī'ah* Committee for Islamic Financial Institutions (1st April 2005). BNM guidelines on Financial Reporting for licensed Islamic Banks (1st July 2005).
2007	BNM guidelines on Corporate Governance for licensed Islamic Banks (24th January 2007).

[263] *Ibid.*
[264] REDmoney, "Islamic Finance News 2011 Guide," (Kuala Lumpur, Malaysia: REDmoney Publication, 2011), 18.
[265] PricewaterhouseCoopers, "*Sharī'ah* Audit: Industry Insight," (Kuala Lumpur, Malaysia: PricewaterhouseCoopers, 2011), 7.

2008	BNM guidelines on Outsourcing for *Takāful* Operators (22nd July 2008).
2009	Amendment of section 51 of Central Bank Act (CBA) to position the *Sharī'ah* Advisory Council of BNM as the apex authority for the determination of Islamic laws for the purpose of Islamic laws for the purpose of Islamic financial business. BNM guidelines on Introduction of New Products. (18th May 2009). BNM guidelines on Introduction of New Products for Insurance Companies and *Takāful* Operators (1st July 2009).
2010	Launch of the new *Sharī'ah* Governance Framework by BNM (effective 1st January 2011). BNM guidelines on Internal Audit Function of Licensed Institutions (1st July 2010). BNM guidelines on Financial Reporting for *Takāful* Operators (23rd December 2010).
2011	By 30 June 2011, IFIs are to comply with the *Sharī'ah* Governance Framework. June 2011: Launch of Phase 2 of the Financial Services Masterplan (FSMP)

Source: PricewaterhouseCoopers (2011), "*Sharī'ah* Audit: Industry Insight."

4.2.2 *Sharī'ah* Framework

It is important for an Islamic finance legal framework to have a robust *Sharī'ah* governance framework to preserve the sanctity of *Sharī'ah* in Islamic finance. This undoubtedly connotes that Islamic finance has its roots in *Sharī'ah*. The most important thing for an Islamic finance is to comply its objectives and operations with *Sharī'ah*. Malaysia's effort in strengthening *Sharī'ah* factors could be highlighted as follows:

- A proper and well-defined governance framework ensures the uniformity and harmonization of *Sharī'ah* interpretations, which aims at strengthening the regulatory framework and promoting good governance within the Islamic financial sector.[266]

- The establishment of two separate bodies of *Sharī'ah* Advisory Councils in Central Bank of Malaysia and Securities Commission Malaysia that function as the authorities and a sole reference of all *Sharī'ah* matters pertaining to Islamic

[266] Malaysia International Islamic Financial Centre, "Primer to Islamic Finance," 27.

banking and *Takāful* as well as the Islamic capital market.[267]

- The requirement for the establishment of a *Sharī'ah* committee within Islamic financial institutions in order to ensure that business operations comply with *Sharī'ah* values and principles.[268]

In Malaysia, the *Sharī'ah* Advisory Council (SAC) of Central Bank of Malaysia monitors the integrity and the credibility of the *Sharī'ah* governance framework. It also functions as a centralized referral body for Islamic finance community, which is by law the *Sharī'ah* Authority of Last Resort in *Sharī'ah* matters relating to Islamic finance.[269]

Among others, the important thing of Islamic finance legal aspect is to ensure good documentation of contracts underlying Islamic financial transactions, which forms an integral part of Islamic finance as it provides a critical 'bridge' between *Sharī'ah* and Islamic finance practices. Such documentation must conform to *Sharī'ah* as its nature as the faith-based system, which enables the "operationalization" of *Sharī'ah* principles into legally enforceable Islamic finance contracts. This is critical to prevent legal risks resulting from the failure in faithfully reflecting the principles of *Sharī'ah*, which could weaken public confidence in the industry.[270]

Another challenge for Islamic finance is in the issue of standardization in Islamic financial transactions. A more standardized contract means a greater certainty and predictability of the characteristics of the financial contracts. Since the late 1990s, the Islamic banking world has commenced efforts to standardize regulation and supervision among Islamic finance countries. The Islamic Development Bank plays a vital role in developing internationally acceptable standards and procedures and

---

[267] *Ibid*., 28.
[268] *Ibid.*
[269] Arab News, "Malaysia Pushing for Islamic Finance Legal Framework," retrieved on 16 October 2011, http://arabnews.com/economy/ islamicfinance/article208977.ece.
[270] *Ibid.*

strengthening the sector's architecture in different countries. Several other international institutions are working to set Sharia-compliant standards and harmonize them across countries. These include the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), the International Islamic Financial Market, the Islamic Finance Service Board (IFSB), the Liquidity Management Centre and the International Islamic Rating Agency.[271] The *Sharī'ah* governance, harmonization and acceptance at the international level is important to lead to the consistency and efficiency and in some instances promote inter-jurisdiction transactions.

4.2.3 Dispute Resolution

4.2.3.1 Judicial System: Dedicated High Court

In order to strengthen the *Sharī'ah* and legal framework, a dedicated High Court has been set up by Malaysia Judiciary, aimed at adjudicating cases involving Islamic banking and *Takāful* in accordance with the existing Malaysian civil laws. Thus, any dispute within or outside the court system that calls into question or issues concerning *Sharī'ah* are referred to the *Sharī'ah* advisory council for guidance and clarification.[272]

In order to preside over litigations relating to Islamic banking and finance, a dedicated judge has been assigned from the commercial division of the Malaysia High Court. At the same time, the SAC in its capacity as a consultative body to the Malaysian judiciary system plays an important role in supporting the court's adjudication in Islamic finance.[273] The Central Bank of Malaysia Act 2009 prevails that if a question concerning to *Sharī'ah* matter arises in any proceeding related to Islamic financial business, where the court or the arbitrator shall take into consideration any published

---

[271] *Ibid.*

[272] Zeti Akhtar Aziz , "Approaches to Regulation of Islamic Financial Services Industry," (Governor of Bank Negara Malaysia-Speech at the IFSB Summit – Islamic Financial Services Industry and The Global Regulatory Environment- The Park Lane Hotel, London, 18 May 2004), 5.

[273] Arab News, "Malaysia Pushing for Islamic Finance Legal Framework," retrieved on 16 October 2011, http://arabnews.com/economy/ islamicfinance/article208977.ece.

rulings of the SAC or refer the matter to the SAC for its ruling. The SAC's rulings are strictly binding on the courts and arbitrators.[274]

4.2.3.2 KL Regional Centre for Arbitration

The Kuala Lumpur Regional Centre for Arbitration (KLRCA) was established in 1978 under the auspices of the international governmental law body, the Asian-African Legal Consultative Organisation (AALCO). This body has been set up to provide a forum for the settlement of disputes by arbitration in trade, commerce and investment within the Asia-Pacific region. The KLRCA gets support from the Malaysian government and function as a non-profit organization and is not a branch or agency of the government.[275]

The Kuala Lumpur Regional Centre (KLRCA) adopts the latest United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules 2010 with some modifications. This rule provides more flexibility in the conduct of proceedings of the arbitration and leaves a wide discretion to the parties with regard to the choice of arbitrators, the applicability of the procedural rules and the place of arbitration.[276]

Specific arbitration rules for Islamic banking and financial services have also been developed to complement the court system. Thus, it would enable disputes for both domestic and international cases to be dealt with by the Kuala Lumpur Regional Centre for Arbitration (KLRCA).[277] Therefore, the 2007 rules of Arbitration (Islamic Banking

---

[274] *Ibid.*
[275] Kuala Lumpur Regional Centre for Arbitration, "Arbitration in Malaysia," retrieved on 26 October, 2011, http://www.klrca.org.my/Arbitration-@-Arbitration_in_Malaysia.aspx.
[276] *Ibid.*
[277] Muhammad bin Ibrahim, "The Polemics of Governing Law in Islamic Finance," 3.

and Financial Services) provide a customised mechanism for the resolution of disputes in the Islamic financial services sector.[278]

The following clause is KLRCA's arbitration to be adopted by any party who wishes to commit any dispute on arbitration under the KLRCA Rules:[279]

"Any dispute, controversy or claim arising from Islamic Banking business, *Takāful* business, Islamic financial business, Islamic development financial business, Islamic capital market products or services or any other transaction business which is based on *Sharī'ah* principles out of this agreement/contract shall be decided by arbitration in accordance with the Rules for Arbitration of Kuala Lumpur Regional Centre for Arbitration (Islamic Banking and Financial Services)."

4.2.3.3 Financial Bureau

The Financial Mediation Bureau (FMB) functions as an independent body set up to help settle disputes between the complainants and his financial service providers who are its members. The consumers could submit claims and complaints to FMB, which provide a platform and timely resolution of disputes. The complaints have a relation to the services provided by the member financial institutions (presently comprising the commercial banks, *Takāful* operators, development financial institutions, Islamic banks, investment banks, insurance companies, and card issuers that are regulated by Central Bank of Malaysia).[280]

4.2.3.4 Law Harmonization Committee

[278] Kuala Lumpur Regional Centre for Arbitration, "Arbitration in Malaysia," retrieved on 26 October 2011, http://www.klrca.org.my/Arbitration-@-Arbitration_in_Malaysia.aspx.
[279] *Ibid.*
[280] *Ibid.*

As part of Malaysia's continuous efforts to further strengthen the legal system and infrastructure to cater for the growing development of the Islamic finance, the Law Harmonisation Committee ("the Committee") has been established.[281]

4.2.3.4.1 Objectives of the establishment

The Committee is established with the following objectives:-[282]

1. To create a conducive legal system that facilitates and supports the development of Islamic finance industry;

2. To achieve certainty and enforceability in the Malaysian laws in regard to Islamic finance contracts;

3. To position Malaysia as the reference law for international Islamic finance transactions; and

4. For Malaysian laws to be the law of choice and the forum for settlement of disputes for cross border Islamic financial transactions.

4.2.3.4.2 Members

Table 4.2: The Committee comprises of the following members:[283]

• *Tun Abdul Hamid Mohamad (former Chief Justice of Malaysia)*	Chairman
• *En. Bakarudin Ishak (Assistant Governor)*	Representing Bank Negara Malaysia
• *En .Kamarolzaman bin Abideen (Deputy Commissioner of Law*	Representing Attorney-General's Chambers

[281] Bank Negara Malaysia, "Law Harmonisation Committee," retrieved on 13 April 2016, http://www.bnm.gov.my/index.php?ch=260&pg=830&ac=861.
[282] *Ibid.*
[283] *Ibid.*

Revision & Reform (Revision)	
• *En. Mohd Radzuan Ahmad Tajuddin (Deputy General Manager and Head of Islamic Capital Market Department)*	Representing Securities Commission
• *Dato' Dr Nik Norzrul Thani (Chairman of Zaid Ibrahim & Co)*	Representing legal fraternity
• *Dr Akram Laldin (Executive Director of International Shariah Research Academy)*	Representing Shariah fraternity
Representative(s) from the industry, whom will be invited on rotation basis.	

The Committee will be supported by a full-time secretariat at Bank Negara Malaysia. In formulating the relevant recommendations, the Committee will consult the Shariah Advisory Councils of Bank Negara Malaysia and Securities Commission Malaysia to seek their views on the Shariah aspect of the recommendations.[284]

4.2.3.4.3 Guiding policy

The Committee aims to ensure due recognition on the Shariah requirements in Islamic finance transactions is accorded in relevant laws affecting the same. It is envisaged that the relevant laws are accommodative and compatible with Shariah requirements.[285]

4.2.3.4.4 Committee's functions

1. To review existing laws with the objective of harmonising the laws to be Shariah compatible, insofar as it is applicable to Islamic finance; and

2. To review new laws that are being made in so far as they affect Islamic finance, to be Shariah compatible.

[284] *Ibid.*
[285] *Ibid.*

4.2.3.4.5 Escalation process

In the course of its review, the Committee welcomes contributions of issues from industry players, legal fraternity, academics and members of the public.[286]

To ensure holistic and comprehensive coverage of issues, further consultations are also expected to be undertaken with identified groups representing Islamic finance industry, legal practitioners and academicians as well as relevant Ministries and regulatory agencies.[287] Recommendations from Committee's deliberations will then be escalated to the relevant Ministries or regulatory agencies for due consideration.[288]

4.3 INITIATIVE 2: THE ESTABLISHMENT OF THE FINANCIAL SECTOR MASTER PLAN

The establishment of the Financial Sector Masterplan (FSMP) was initiated by Central Bank of Malaysia (CBM) through a joint team involving a number of departments in CBM. An advisory industry group that consists of the Chief Executive Officers and the Managing Directors of selected institutions has been set up to consult views from the industry side. The consultations also involve relevant ministries and Government agencies, industry players and other key stakeholders on the certain recommendations in the FSMP. This approach was taken to gain most viable options in achieving the strategic direction and clear objectives of the plan. Several series of workshops/meetings/interviews were pursued with industry players on related issues. Survey and data analytical approach method had been conducted to gather information from various parties, where it proceeded through external and internal interviews to identify the critical gaps in the financial system and cross country comparison of alternative financial structures and liberalization paths, define key success factors in

[286] *Ibid.*
[287] *Ibid.*
[288] *Ibid.*

financial market development and formulate alternative end games for the Malaysian financial system.[289]

The FSMP is designed to set out the plan to outline future direction of the financial system for the next 10 years that will ensure its continued effectiveness and resilience.[290] Thus, the objective of FSMP formally is "to develop a more resilient, competitive and dynamic financial system with best practices, that supports and contributes positively to the growth of the economy through the economic cycle, and has a strong core and forward looking domestic financial institutions that are more technology-driven and ready to face the challenges of liberalization and globalization."[291] Among other initiatives in the plan are to lay out strategies to enhance Malaysia's Islamic banking and insurance sectors and international offshore financial center and supporting institutions as well as to venture capital firms, in its aim to promote a well-diversified financial sector.

The FSMP, which was released in early 2001 consists of three gradual phases of implementation and aims to improve efficiency, resilience innovation, flexibility and dynamism in the banking system. There are 119 recommendations in the financial sector master plan. The implementation of the recommendations will observe the following approach and safeguards:

4.3.1 PHASE I

The primary target in the transition is to build up a core of strong domestic banking institutions. Thus, initial step is to strengthen the capability and capacity of domestic banking institutions, to create an environment where the best domestic

---

[289] Bank Negara Malaysia, *Financial Sector Master Plan (FSMP)*, (Kuala Lumpur, Malaysia: Bank Negara Malaysia, 2010), 7.
[290] *Ibid.*, 15.
[291] *Ibid.*, 16.

banking institutions emerge and enhance the financial infrastructure.[292] By the fourth year, the Islamic banking system is expected to be strong enough for competition with other banking systems.

4.3.2 PHASE II

After the first phase of strengthening domestic banking institutions was completed and had greater capacity and capability to compete, the playing field for foreign players will increasingly be leveled.[293] Previous restrictions over the incumbent foreign banks will be removed such as permitting them to share automated teller machines (ATM) networks with local banks.

4.3.3 PHASE III

This phase is considered as the beginning of a new foreign competition. This is the result of the intensifying degree of global competition and greater assimilation into the global arena. Thus, domestic banking sector needs to be prepared for greater liberalization.[294] This phase started in the seventh year (in 2007) when Malaysia opened up its banking industry to new international players in line with the World Trade Organization (WTO) liberalization program.

The liberalization of Malaysia's Islamic banking market commenced with the opening of the first foreign Islamic bank in August 2005. Subsequently, all Islamic banking windows converted into full-fledged of Islamic banks in 2007 as reflected in the increase of domestic focus on Islamic banking business, supported by clearer accountabilities under separate Board and management structures.[295]

---

[292] *Ibid.,* 36.
[293] *Ibid.*
[294] *Ibid.*
[295] PricewaterhouseCoopers,"*Malaysia, Asia's Islamic Finance Hub*," 37.

For the time being, Malaysia has 17 full-fledged Islamic banks and seven participating commercial banks in the Islamic banking scheme (Islamic banking windows in commercial banks). Among others, the financial institutions offering Islamic banking services include six investment banks and one international Islamic bank. Three of the full-fledged Islamic banks are foreign-owned banks. They are the Kuwait Finance House (Malaysia) Bhd., Al-Rajhi Banking & Investment Corporation (Malaysia) Bank Bhd. and Asian Finance Bank Bhd. There are also six development financial institutions offering Islamic banking services.[296] In May 2008, another two additional full-fledged Islamic banks licenses had been approved. For example, Maybank Islamic Bhd. and Alliance Islamic Malaysia Bank Bhd. [297]

The liberalization policy could drive the government's initiative to promote structural change within the economy and broaden the sources of growth to further drive economic expansion. In economy, the financial services sector is an integral component, and has increased its share in GDP (gross domestic product) from 9.2 percent in 2000 to 11 percent in 2008. It is estimated that more than 140,000 workers are employed by banking institutions and insurance companies in Malaysia. It shows the successful function of FSMP, which achieved its target timely as outlined by Central Bank of Malaysia, since its inception in 2001. Indeed, based on Central Bank of Malaysia report, some 90 percent of the FSMP initiatives have been completed.[298]

Under the new liberalization measures, the Central Bank of Malaysia will issue:

- up to two new Islamic banking licenses in 2009 under the Islamic Banking Act 1983 to world class foreign players to establish new Islamic banks.

[296] *Ibid.*
[297] *Ibid.*
[298] Arab News," Malaysia liberalizes financial sector for foreign players," retrieved on 20 October 2011, http://archive.arabnews.com/ ?page=6&section=0&article=122189&d=4&m=5&y=2009.

These banks can be 100 percent foreign-owned and must have a paid-up capital of at least $1 billion.

- up to two new family *Takāful* (Islamic insurance) licenses in 2009 to players that can offer significant value proposition to Malaysia to spur the development of the *Takāful* industry.

In order to facilitate a foreign entity with freer space to move, the government has also changed the ceilings for foreign equity ownership in onshore Malaysian Islamic banks, investment banks, insurance companies and *Takāful* operators from 49 percent to 70 percent. This policy resulted in the increment of shares entitles to be owned by foreign shareholders in Malaysian financial institution in the above categories, where it does not include commercial domestic Malaysian banks where the foreign equity shareholding remains at the current 30 percent. When this happens, there must be a minimum of $1 billion paid-up capital.[299]

Based on the Central Bank of Malaysia's view, the liberalization must also be accompanied with sufficient safeguards to ensure intact, effective and sound financial system in Malaysia. To preserve the resilience of the financial system, capacity and institutional building efforts will continue to be pursued, complemented by enhancements of the supervisory, regulatory and surveillance framework.[300]

This liberalization effort makes Malaysia the most open market for Islamic banking and finance around the world and reinforces Kuala Lumpur’s leadership in the sector. The liberalization challenge remains to other Islamic countries such as Bahrain,

---

[299] *Ibid.*
[300] *Ibid.*

Saudi Arabia, the UAE, Turkey, Qatar and Kuwait to take up their markets for foreign investors.[301]

4.3.4 Financial Sector Masterplan Success (FSMP)

In 2009, the Governor of Central Bank of Malaysia, Tan Sri Zeti Akhtar Aziz announced the success of FSMP as she quoted in *StarBiz*: "*We are pleased that within nine years, more than 90% of the recommendations have been implemented*." Thus, through the FSMP recommendations, Malaysian banking institutions have successfully developed their scale to become superior in Islamic finance and regional champions. With the objective to build meaningful size, a greater specialization and convergence was targeted. The distance between local and foreign banks has lessened considerably, with more product and services offered by many local banking groups, which are competitive with those offered by the locally incorporated foreign banks.[302]

Under the FSMP, the development of electronic payment channels and usage of information technology in the Malaysian banking sector had seen many improvements. There was also an enhancement in credit skill building measures and development of industry-wide benchmarks, which were highlighted under the master plan. Among other successes of FSMP; many measures including increased supervision, ascribing ratings on banks and risk weightings on capital and loans had been set up in place.

In lieu of the successes, many of these measures worked in many economic conditions especially in the situation of the global financial turmoil, which enabled Malaysian banking institutions relatively unscathed. In the financial market sector, the mergers of stockbroking houses and merchant banks had resulted in the creation of full-fledged Islamic investment banks, attracted many new interested investors to take advantage from the improving capital markets. The presence of new non-traditional

---

[301] *Ibid.*

[302] The Star, "New Blue Print for Financial System Expansion Likely," retrieved on 20 September 2011, http://biz.thestar.com.my/ news/story.asp?file=/2009/8/6/business/4464176&sec=business.

players is also considered an upcoming force as better value propositions coloured new face of ever-discerning Malaysian consumers. Following the existence of new consumers and the shift towards an increasingly deregulated banking sector, the CBM has taken necessary action to ensure higher consumer protection.[303] In the area of human resource development, some issues such as staff mobility and talent attraction are something critical components that the authority should take into account. The new structure of ownership in Malaysian banking institutions had also undergone significant transformation with the emergence of institutional and foreign investors.

4.4 INITIATIVE 3: THE ESTABLISHMENT OF MALAYSIA INTERNATIONAL ISLAMIC FINANCIAL CENTRE (MIFC)

The Malaysia International Islamic Financial Centre (MIFC) initiative was launched in August 2006 with the objective to promote Malaysia as a major hub for international Islamic finance. Several parties who are involved in this initiative are a community network of financial and market regulatory bodies, financial institutions, government ministries and agencies, human capital development institutions and professional services companies that are participating in Islamic finance.[304]

The emergence of MIFC initiative on 14 August 2006 was timely amidst a strong foundation and steady performance of the Islamic financial industry in Malaysia. It indicated the inception of a new stage for the future landscape of the Islamic financial system in the country. Several prominent measures were highlighted to initiate the MIFC program. It was aimed at positioning Malaysia as a centre for Islamic financial products and services in international currencies to the global and domestic financial communities. This effort presented new prospects and business opportunities for

[303] *Ibid.*

[304] The Malaysia International Islamic Financial Centre (MIFC), "Introduction," retrieved on 27 October 2011, http://www.mifc.com/index.php?ch=menu_ exp&pg=menu_exp_ovr&ac=37&ms=1.

financial institutions to realize the potential of evolving a vibrant Islamic financial hub.[305]

The setting up of MIFC involved several authorities and regulators, namely BNM, SC, Labuan Offshore Financial Services Authority (LOFSA) and Bursa Malaysia. This collective work aimed at providing an integrated and comprehensive approach to the development of MIFC. The MIFC objectives, among others are to develop Malaysia into a centre for the origination, distribution and trading of Islamic capital market instruments, for example, treasury instruments, *Sukuk*s as well as Islamic fund and wealth management. Products and services under the MIFC are available in any currency and can be offered to both residents and non-residents.[306]

MIFC functions as one of the key intermediation linkages with the global market place and plays important roles in accelerating the process of bridging and strengthening the relationship between the international Islamic financial markets, and thereby expand the investment and trade relations between the Middle Eastern, West Asia and North Africa regions with East Asia.[307] For MIFC promotion, CBM has introduced several new offshore Islamic banking and *Takāful* licenses as follows:

- International Islamic Bank (IIB) license to conduct international banking businesses in international currencies.

- International *Takāful* Operator (ITO) license to conduct international *Takāful* businesses in international currencies.

[305] Zeti Akhtar Aziz, "Malaysia as an International Financial Centre," (Keynote address by the Governor of Central Bank of Malaysia, at the dialogue with Industry participants on MIFC (Malaysia International Islamic Financial Centre, Kuala Lumpur, 1 November 2006), 2.
[306] PricewaterhouseCoopers,"*Malaysia, Asia's Islamic Finance Hub*," 20.
[307] Bank Negara Malaysia, "MIFC," retrieved on 21 October 2011, http://www.bnm.gov.my/index.php?ch=9&pg=15&ac=232.

- Existing Islamic banks and *Takāful* operators can set up International Currency Business Units (ICBUs) to conduct the full range of Islamic banking or *Takāful* services with non-residents and residents in international currencies.

- Flexibility for Labuan Offshore Islamic banks, Islamic divisions of the offshore banks as well as offshore *Takāful* operators to open offices anywhere in Malaysia.

In the meantime, SC has initiated the establishment of Islamic fund management services in Malaysia. The government is keen on the effort to create the necessary critical mass of players and increase the scale of Islamic finance activities.[308]

In addition, *Sharī'ah* governance plays a vital role in the development of Islamic finance. Thus, it drives to the right order and compliance with the Islamic injunctions, thereby ensuring customer's confidence. Malaysia also enjoyed a *Sharī'ah* environment that is conducive, which helps to sustain Malaysia as a centre of product innovation and producing cutting-edge product for the increasingly sophisticated customers. In respect of *Sharī'ah* interpretation and practices, the MIFC will adopt a stance of mutual recognition between different rulings and deliberations and accommodate to various juristic reasoning approved by recognized *Sharī'ah* advisers.[309]

The MIFC Executive Committee has been formed following the streamline of the associated delivery system by the government to facilitate advancing MIFC agenda. The Committee consists of a high level of 28 groups of top officials from the key relevant Ministries, Government departments and agencies, financial and market regulators and representatives from the banking and *Takāful* sectors. This Committee

[308] PricewaterhouseCoopers,"*Malaysia, Asia's Islamic Finance Hub*," 20.
[309] Zeti Akhtar Aziz, "Malaysia as an International Financial Centre,"2.

is obliged to provide the direction as well as undertaking a review of all present policies that are related to the comprehensive and coordinated promotion of the MIFC.[310]

The secretariat, formed by Central Bank of Malaysia, will serve as the Executive Committee and act as a single contact point for the implementation of the MIFC initiatives. This committee is supported by a group of working level committees to undertake the task of considering new proposals and observing the implementation of the MIFC recommendations. An International Advisory Panel (IAP) is also being formed comprising industry leaders and experts from the global community for the consultation on the global trends and to provide insights on the strategic direction.[311]

4.4.1 Conducive Environment for Business

In creating an environment for the efficient functioning of the MIFC, the Government has made a strategic decision by granting an attractive tax package to promote Malaysia as a competitive international Islamic financial centre. The objective is to create the necessary critical mass of participating financial players and to increase the scale of activity. Malaysia aims to attract global players and to enhance the capabilities of the existing financial institutions.

Among the measures that have been introduced are: [312]

- First, liberalizing the Islamic Banking and *Takāful* and re-*Takāful* markets through the issuance of new licenses for foreign participation.

- Second, allowing foreign equity ownership of up to 49 percent in existing Islamic banks and *Takāful* companies.

[310] *Ibid*.
[311] *Ibid*.
[312] *Ibid*.

- Third; the issuance of International Islamic Bank and International *Takāful* Operator licenses under the Islamic Banking Act and the *Takāful* Act respectively to qualify foreign and Malaysian financial institutions to conduct the full range of Islamic banking business or *Takāful* and re*Takāful* business in international currencies and enjoy tax holiday for 10 years under the Income Tax Act starting from the year of assessment 2007.

- Fourth, granting approval to Malaysian Islamic banks and *Takāful* operators to set up the International Currency Business Unit (ICBU) to offer Islamic financial services in international currencies and enjoy similar tax holiday.

- Fifth, provide a greater flexibility to the Labuan offshore entities offering Islamic financial services to open operation offices anywhere in Malaysia. The Labuan tax law will continue to be applied to these players.

With regard to the new Islamic finance players, they are given two options under MIFC program, either by being licensed under Central Bank of Malaysia to benefit from the tax holiday for 10 years under the Income Tax Act and fully benefit from the Double Tax Agreement, or to be licensed under the Labuan Offshore Financial Services Authority (LOFSA) and be taxed accordingly under the Labuan offshore Business Activity Tax Act.[313]

Other primary objective of MIFC is to promote Malaysia as the preferred choice of the centre offering Islamic financial services. This vision is associated with the building of talent and expertise and with the creation of sound environment of cost competitive and conducive for product innovation and product offering. The measures to address this, include:[314]

313 *Ibid*.
314 *Ibid.*

- First, setting up the International Centre for Education in Islamic Finance (INCEIF).

- Second, establishing a *Sharī'ah* Endowment Fund for scholarships, research and international *Sharī'ah* dialogues for the regional and international *Sharī'ah* communities to enhance the harmonization of *Sharī'ah* interpretation and practices.

- Third, an additional 20 percent exemption in stamp duty on Islamic financial instruments on top of the stamp duty exemption that is currently available to ensure tax neutrality.

- Fourth, encouraging Malaysian-owned banks including Islamic financial institutions to expand their operations abroad by allowing the profits of the newly established branches overseas or remittances of new overseas subsidiaries to be given income tax exemption for 5 years.

- Fifth, liberalizing the foreign exchange administration rules to allow multilateral development banks and multinational corporations to issue ringgit denominated instruments in our domestic bond market.

At the international level, Malaysia has gained recognition upon its continuous efforts in strengthening the Islamic financial system domestically and internationally. A primary objective as announced is to enhance the position of Malaysia as a leading international Islamic financial centre. As Malaysia is located in the central Asian time zone, it is a benefit for Malaysia to effectively serve the East Asian region.[315]

[315] Ministry of International Trade and Industry (MITI), "The Banking System in Malaysia," retrieved on 20 October 2011, http://www.miti.gov.my/cms/content.jsp?id=com.tms.cms.section.Section_64594899-c0a8156f-5cff5cff-2b0aba2c.

A royal award has been introduced by Malaysian government in honoring the exceptional individual for outstanding contribution to global Islamic finance.[316] The award is named as "The Royal Award for Islamic Finance," after getting consent by His Majesty Yang di-Pertuan Agong of Malaysia. The Royal endorsement, which was spearheaded by the Malaysia International Islamic Financial Centre (MIFC) initiative, has given a prestige value to the award.[317]

MIFC has gained the International recognition in 2009, indicated its strong position as a major hub for international Islamic finance. In the same year, MIFC was once again selected as the 'Best International Islamic Finance Centre 2009' at the Annual London *Sukuk* Summit Awards of Excellence and then awarded as the 'Islamic Finance Hub of the year 2009' by The Asset Magazine. The Central Bank of Malaysia (CBM) was also awarded the 'Best Central Bank in Promoting Islamic Finance' at the Islamic Finance Awards in 2009. MIFC continuously received recognition in the following year, when awarded as the "Best International Islamic Finance Centre" at the Annual London *Sukuk* Summit Gala Dinner and *Sukuk* Summit Awards.[318]

4.5 INITIATIVE 4: MALAYSIA'S GOVERNMENT SUPPORT: TAX INCENTIVES

The Malaysian Government plays vital roles to promote Malaysia as an International Islamic financial centre, by giving substantial tax incentives in the area of Islamic finance.[319] In the effort to facilitate the Islamic finance market and transactions in Malaysia, the Government has made changes to the tax regime to streamline the tax

[316] Bank Negara Malaysia, "Malaysia's Royal Award for Islamic Finance," retrieved on 21 July 2011, http://www.bnm.gov.my/ index.php?ch=8&pg=14&ac=2090.
[317] *Ibid.*
[318] Malaysia International Islamic Financial Centre, retrieved on 20 October 2011, http://www.mifc.com/ index.php?ch=seg_tal_pro&pg=seg_ tal_pro_ovr.
[319] PricewaterhouseCoopers,"*Malaysia, Asia's Islamic Finance Hub*," 55.

structure on Islamic finance transactions.[320] Amendments were made to the Income Tax Act 1967, the Real Property Gains Tax Act 1976 and the Stamp Act 1949. Under the tax neutrality framework, special treatment is given for additional instruments and transactions in fulfilling *Sharī'ah* requirements, where there are no additional stamp duty and tax payments.[321]

Such treatment is also adopted in the Islamic banking and finance, where there is no income tax on income earned from Islamic banking and *Takāful* businesses traded in foreign currencies by the International *Takāful* Operator (ITO), International Islamic Bank (IIB), and International Currency Business Unit (ICBU) under the MIFC initiative. Therefore, no stamp duty charge is imposed on any activity related to Islamic Banking and *Takāful* in foreign currencies.[322]

For the Islamic Capital Market, tax deduction policy is exercised on expenses incurred in the issuance of Islamic securities approved by the Securities Commission Malaysia. Stamp duty exemption is also exercised on Islamic securities instruments issued in any currency as approved by the Securities Commission Malaysia. As for Islamic Fund management, local and foreign companies are exempted from income tax charges on management fees for local and foreign companies managing approved Islamic funds for both local and foreign investors.[323]

The following table specifically highlights the tax deduction incentives by the Malaysian government.

Table 4.3: Tax Deduction Incentives

[320] *Ibid.*, 57.
[321] *Ibid.*, 57.
[322] Malaysia International Islamic Financial Centre, "Primer to Islamic Finance," 32.
[323] *Ibid.*

Facilitation of financing transactions	The definition of partnership for tax purpose is very wide and includes all types of partnerships. Hence, any type of partnership, unless specifically excluded, would have to file tax returns. In recognizing and promoting Islamic financing structures based on the concept of *Mushārakah* or Mudhārabah, such financing transactions need not file partnership tax returns. This is effective from YA 2007.
Tax exemption of fund managers	Effective from YA 2008 – YA 2016: 10-year tax exemption for local and foreign companies managing funds established under the *Sharī'ah* principles and approved by SC.
Real Estate Investment Trusts (REITs)	REITs have also been provided with further boost through several tax initiatives: • So long as REITs distribute at least 90% of income to investors, the REITs will not have to pay tax. • Distributions to certain investors will be subject to reduced tax for five years, namely: • Non-corporate investors, including resident and non-resident individuals, that receive dividends from approved REITs, be subject to a final withholding tax of 15%; and • Foreign institutional investors, especially pension funds and collective investment funds, that receive dividends from approved REITs, be subject to a final withholding tax of 20%. Corporate investors (resident and non-resident) will continue to be subject to normal corporate income tax at 26% (to be reduced to 25% from YA 2009).
Human capital	In encouraging Malaysians to explore Islamic finance as a career choice, tax relief not exceeding RM5,000 (US$1,552) p.a. is also provided on Islamic finance courses approved by BNM or SC at local institutions.
Extension of tax deduction on issuance costs of Islamic securities	Extension of three years to 2010, tax deduction on the expenses incurred on the issuance of Islamic securities based on *Ijārah*, Istisna', Mudhārabah, Mushārakah and other Islamic securities.
Stamp duty	Further stamp duty exemption of 20% on instruments used in Islamic financing products approved by the SAC of BNM or SC for a period of three years, up to 31 December 2009. This means that Islamic transactions will suffer less stamp duty by 20% compared to conventional financing instruments. 100% stamp duty exemption for 10 years up to 31 December 2016 on foreign currency instruments executed by International Currency Islamic financial institutions.
Others	Other tax initiatives include: • Pre-commencement expenses of an Islamic stockbroking business will be allowed as tax deduction so long as business is commenced within two years from the approval by SC. Applications have to be received by SC from 2 September 2006 to 31 December 2009. • Special purpose vehicles established solely for the purposes of issuance of Islamic bonds need not to be subject to tax or tax

	administrative procedures, subject to certain conditions.

YA: Year Assessment

Source: Malaysia International Islamic Financial Centre (2008), 'Primer to Islamic Finance, Central Bank of Malaysia, Kuala Lumpur.

4.6 INITIATIVE 5: STRENGTHENING SHARĪ'AH FACTORS

4.6.1 *Sharī'ah* Advisory Council

Malaysia has established *Sharī'ah* advisory body named as the *Sharī'ah* Advisory Councils for the Islamic banking and *Takāful* sectors as well as for the Islamic Capital Market (ICM). The *Sharī'ah* Advisory Councils of Central Bank of Malaysia was formed with an objective to advise on matters in relation to Islamic banking and *Takāful* businesses or any other Islamic finance area that is supervised and regulated by BNM. The *Sharī'ah* advisory Council of the Securities Commission Malaysia (SC) functions to advise on matters pertaining to the Islamic Capital Market. The two SAC members are participated by a group of prominent scholars, jurists and market practitioners function in providing *Sharī'ah* opinions and have a vast experience in banking, finance, economics, law and application of *Sharī'ah*, especially in the areas of Islamic economics and finance.[324]

The *Sharī'ah* Advisory Council of Central Bank of Malaysia (SAC) was established in May 1997 and supervised by Central Bank of Malaysia. The SAC is recognized as the highest *Sharī'ah* authority in Islamic finance in Malaysia and authorized for the ascertainment of Islamic law for the purposes of Islamic banking business, *Takāful* business, Islamic financial business, Islamic development financial business or any other business, which is based on *Sharī'ah* principles. The SAC is also responsible for validating all Islamic banking and *Takāful* products to ensure their compliance with the *Sharī'ah* principles as well as advising Central Bank of Malaysia on any *Sharī'ah* issue related to Islamic financial business or transactions of Central

[324] Malaysia International Islamic Financial Centre (MIFC), "*Sharī'ah* Advisory Council (SAC)," retrieved on 26 October 2011, http://www.mifc.com/index.php?ch=menu_ law&pg=menu_law_sac.

Bank of Malaysia or other related entities.[325] Other roles of SAC are to ensure that banks comply with the shari'ah rules and guidelines. For this purpose, SAC is responsible to study and analyze the shari'ah opinions of the *Sharī'ah* Supervisory Committee (SSC) of Islamic banks and financial institutions. Central Bank of Malaysia has prepared the *Guidelines on the Governance of Sharī'ah Committee* for the Islamic Financial Institutions or known as *BNM/GPS 1* that regulates the governance of *Sharī'ah* Committee of an Islamic financial institution.[326]

4.6.1.1 National ***Sharī'ah*** Advisory Council to Have Final Say

The role and functions of the SAC were further reinforced in the Central Bank of Malaysia Act 2009, whereby the SAC was accorded as the sole authoritative body on *Sharī'ah* matters pertaining to Islamic banking, *Takāful* and Islamic finance. The rulings of the SAC shall prevail over any contradictory ruling given by a *Sharī'ah* body or committee constituted in Malaysia as well as in any proceedings related to Islamic financial business, where the court and arbitrator are also required to refer to the rulings of the SAC.[327]

The reason for the amendment of previous ruling is due to the several cases of unwilling judges to prevail the deliberation of *Sharī'ah* Advisory Council as their reference. This action has caused different views from what has been deliberated by the SAC. One of the dispute cases involved is highlighted as follow:

Raus Sharif JCA when delivering judgment in the case of Bank Islam Malaysia v. Lim Kok Hoe and Anor and Other Appeals (2009) 6 CLJ 22 on page 39 stated that:[328]

---

[325] Bank Negara Malaysia, "*Sharī'ah* Advisory Council of the bank," retrieved on 26 October 2011, http://www.bnm.gov.my/index.php?ch=7&pg=715&ac=802.

[326] Bank Negara Malaysia, "Guidelines on the Governance of *Sharī'ah* Committee," retrieved on 26 October 2011, http://www.bnm.gov.my/ guidelines/01_banking/04_prudential_stds/23_gps.pdf.

[327] Bank Negara Malaysia, "*Sharī'ah* Advisory Council of Bank Negara Malaysia," retrieved on 30 October 2011, http://www.bnm.gov.my/index.php?ch=7&pg=715&ac=802.

[328] Surianom Miskam, "Reference to The *Sharī'ah* Advisory Council in Islamic Banking and Finance Cases: The Effect of the Central Bank of Malaysia Act 2009," (Paper Proceeding in International Conference on Business and Economics Research (ICBER), at Hilton Hotel, Kuching Sarawak, 15-16 March 2010). 4.

"*The Court will have to assume that the Sharī'ah advisory body of the individual bank and now the Sharī'ah Advisory Council under the aegis of Central Bank of Malaysia, would have discharge their statutory duty to ensure that the Sharī'ah Advisory Body of BIMB or the Sharī'ah Advisory Council established by Bank Negara had failed to exercise their statutory duties. Thus the learned judge, with respect, should not have taken upon himself to rule that the BBA contracts were contrary to the Religion of Islam without having any regard to the resolutions of the Sharī'ah Advisory Council of the Central Bank Malaysia and the Sharī'ah Advisory Council body of BIMB on the validity of BBA contracts.*"

The learned judges of the court of Appeal for the case agreed with the observation made earlier by Suriyadi Halim Omar J in the case of Arab Malaysian Merchant Bank Bhd. V Silver Concept Sdn. Bhd. [2006] 8 CLJ9 and ruled that judges in civil courts should not take upon themselves to declare whether a matter is in accordance to the religion of Islam or otherwise. Thus, the eligible party to decide whether the bank business is in accordance with the religion of Islam is the eminent jurists who are properly qualified in the field of jurisprudence.[329]

Thus, the newly passed Central Bank of Malaysia Act 2009 granted the power of the *Sharī'ah* Advisory Council as the highest and sole authority to be referred to by the civil courts in dealing with Islamic banking and finance cases and disputes in Malaysia.[330]

4.6.2 *Sharī'ah* Committees

The establishment of the *Sharī'ah* Committee in an Islamic financial institution is compulsory. In some cases such as the case of the BAFIA IBS bank, it may establish a *Sharī'ah* Committee for the banking group. However, if *Takāful* operator is part of

[329] *Ibid.*
[330] *Ibid.*

that group, it is compulsory for *Takāful* operator to establish its own separate *Sharī'ah* Committee, as required in *Takāful* Act (TA).[331]

The *Sharī'ah* committee's duties and responsibilities among others are to advise the board on *Sharī'ah* matters in its business operation, to endorse *Sharī'ah* Compliance Manuals, to endorse and validate relevant documentations, to advise on matters to be referred to the SAC, to assist related parties on *Sharī'ah* matters for advice upon request, to provide written *Sharī'ah* opinion and to assist the SAC on reference for advice.[332]

4.6.3 *Sharī'ah* Audit and Review

The primary objective of *Sharī'ah* audit is to provide assurance to stakeholders independently by ensuring compliance with *Sharī'ah*, comprising the products and services provided by Islamic financial institutions and *Takāful* operators. The *Sharī'ah* audit is to be performed critically by eminent internal auditors who have adequate *Sharī'ah*-related knowledge and skills. Their supreme goal is to guarantee a sound and effective internal controls system for *Sharī'ah* compliance. Internal auditors may also consist of the experts among Islamic Finance Institution's *Sharī'ah* officers, as long as the objectivity of the audit is not compromised. In some cases, IFIs may also appoint an external party to conduct a *Sharī'ah* audit on their banking operations.

There are three approaches for *Sharī'ah* audit:[333]

1. Audit of IFIs' financial statements: Independent assessment and objective assurance to ensure an effective internal control system for *Sharī'ah* Compliance.[334]

---

[331] Laws of Malaysia, Act 276, Islamic Banking Act 1983, 4.
[332] *Ibid*., 9.
[333] PricewaterhouseCoopers, "*Sharī'ah* Audit: Industry Insight," 8.
[334] Bank Negara Malaysia, "Guidelines of *Sharī'ah* Governance Framework," retrieved on 26 October 2010, http://www.bnm.gov.my/guidelines/05_*Sharī'ah*/02_*Sharī'ah*_Governance_ Framework_ 20101026.

2. Compliance audit on organizational structure, people and processes: *Sharī'ah* audit covers all aspects of business operations and activities.[335]

3. Review on the adequacy of the *Sharī'ah* governance process: To provide recommendations and results to Audit Committee and *Sharī'ah* Committee.[336]

4.6.4 *Sharī'ah* Parameter

On 28 August 2009, Central Bank of Malaysia announced the issuance of the *Sharī'ah* Parameter Reference 1 or *Murābahah* Parameter (SPR1). This Parameter applies to all Islamic financial institutions under the purview of Central Bank of Malaysia. SPR1 is the first *Sharī'ah* Parameters issued as a guidance and reference to all Islamic financial institutions. The remaining *Sharī'ah* Parameters currently being developed are *Ijārah*, *Mudhārabah*, *Mushārakah*, *Istisnā'* and *Wadī'ah*. The SPR1 has been endorsed by Central Bank of Malaysia's *Sharī'ah* Advisory Council and become the first point for Bank's future progress in the effort to promote a greater development of the Islamic finance industry.[337]

The *Sharī'ah* Parameters initiative aims at defining the essential features of Islamic financial products and services based on the underlying *Sharī'ah* contracts that are endorsed by the *Sharī'ah* boards and adopted by Islamic financial institutions. The issuance of *Sharī'ah* Parameters as standard documents will facilitate comprehensive understanding of the principles and the basis for adopting *Sharī'ah* contracts. The other objectives of the parameters include:

---

[335] *Ibid.*
[336] *Ibid.*
[337] Bank Negara Malaysia, "The Issuance of *Sharī'ah* Parameter Reference 1 (Murabahah Parameter) to Promote Harmonisaton of Practice," retrieved on 12 August 2011, http://www.bnm.gov.my/index.php?ch=8&pg=14&ac=1907.

1. To clarify the concepts, principles and conditions of *Sharī'ah* contracts;
2. To provide the focus on the features of *Sharī'ah* contracts that form the basis of Islamic financial products and services;
3. To provide the basis for decisions on matters related to conditions, mechanisms and the implementation of *Sharī'ah* contracts;
4. To facilitate Islamic finance professionals and practitioners in the design and development of Islamic financial products and services; and
5. To facilitate the formulation of policies and guidelines on contracts adopted by the Islamic financial services industry.

The SPR1 will serve as an important reference document, particularly for Islamic financial institutions, *Sharī'ah* advisors, academics, researchers, students and members of the public who have interest in Islamic finance. SPR1 outlines the main *Sharī'ah* requirements in the contracts and provides examples, methods and models for the practical application of the contract. In addition, the SPR1 would contribute to further harmonization in the interpretation and application of *Sharī'ah* views and opinions, especially among *Sharī'ah* Committee Members. In this regard, the *Sharī'ah* parameter document provides an important reference for *Sharī'ah* Committee Members to arrive at *Sharī'ah* decisions pertaining to Islamic financial transactions, products and services.[338]

Several studies surveyed the local and international Islamic banking boards and compilation of various fatwas undertaken by Central Bank of Malaysia to ensure the robustness of the *Sharī'ah* parameter. The concept paper was presented to the *Sharī'ah* Advisory Council of Central Bank of Malaysia for review and approval and was

[338] *Ibid*.

subsequently circulated among the industry, academia, international bodies and other relevant stakeholders for feedback and comments.[339]

4.6.5 *Sharī'ah* Standards

Sharī'ah Standards is the new brand name for Shariah Parameters. The *Sharī'ah* Standards is issued pursuant to section 59 of the Central Bank of Malaysia Act 2009. The purpose of *Sharī'ah* Standards is to provide standard on features of *Sharī'ah* contracts applicable in Islamic financial transactions. The document facilitates the understanding of a particular *Sharī'ah* contract requirement. The required and optional features specified in the Standards shall serve as standards for the Islamic financial institution to apply a particular *Sharī'ah* contract in developing Islamic financial products and services. The Standards is expandable to address the dynamism of Islamic finance activities.[340]

The first standard issued by the Central Bank of Malaysia was on Murabahah standard. Overall standards are 11 standards which function to complement existing *Sharī'ah* guidelines issued by the Central Bank of Malaysia, as the regulator aims to address inconsistencies in the use of Islamic contracts.[341]

The *Sharī'ah* Standards is issued in accordance to rulings of the *Sharī'ah* Advisory Council (SAC) of Bank Negara Malaysia. It is a published ruling of the SAC. IFIs shall refer to *Sharī'ah* Standards document in applying a particular *Sharī'ah*

---

[339] *Ibid.*

[340] Bank Negara Malaysia,"The Principles of Shariah in Islamic Finance: Shariah Standard on Mudarabah," retrieved on 10 April 2016, http://www.bnm.gov.my/guidelines/05_shariah/shariah_std_ mudarabah.pdf.

[341] Malaymailonline, "Bank Negara Isssues New Guidance to Tackle Uneven Islamic Finance Practices, retrieved on 10 April 2016, http://www.themalaymailonline.com/money/article/bank-negara-issues-new-guidance-to-tackle-uneven-islamic-finance-practices#sthash.S3kXKIaY.dpuf

contract as part of its implementation of *Sharī'ah* compliance function outlined in the "*Sharī'ah* Governance Framework for Islamic Financial Institutions."[342]

4.6.6 Developing *Sharī'ah* Governance Framework

The *Sharī'ah* Governance and *Sharī'ah* Audit are essential elements of Islamic Financial Institutions (IFIs). The Central Bank of Malaysia (CBM) has introduced a comprehensive *Sharī'ah* Governance Framework (SGF), which came into force in January 2011. The SGF concept is similar to the Guiding Principles on *Sharī'ah* Governance Framework for Islamic Financial Institutions as issued by Islamic Financial Services Board (IFSB) and formulated specifically to enhance the role of the Board, *Sharī'ah* Committee and the Management of IFIs, especially in respect of *Sharī'ah* Audit, *Sharī'ah* Review, *Sharī'ah* Risk Management and *Sharī'ah* Research.[343]

With the issuance of the new framework, the previous 2004 guidelines on the governance of the *Sharī'ah* committee for Islamic Financial Institutions were automatically revoked. The primary objective of the new framework is to enhance the role of the *Sharī'ah* board, committee and institution's management in relation to *Sharī'ah*. Another benefit from this new framework is that it is expected to enhance relevant departments with responsibility in attaining a *Sharī'ah*-based operating environment. In addition, it seeks to propose the functions of *Sharī'ah* review, auditing, risk management and research.[344] The framework is also used to define the expected level of accountability and responsibility towards various parties such as the board of

---

[342] Bank Negara Malaysia,"The Principles of Shariah in Islamic Finance: Shariah Standard on Mudarabah," retrieved on 10 April 2016, http://www.bnm.gov.my/guidelines/05_shariah/shariah_std_ mudarabah.pdf.

[343] International *Sharī'ah* Research Academy for Islamic Finance (ISRA), "International *Sharī'ah* Audit Conference," retrieved on 1 November 2011, http://www.isra.my/events/events-calendar/details/5-international-*Sharī'ah*-audit-conference-2011-isac2011.html.

[344] *Ibid*.

directors, the *Sharī'ah* board and the management of Islamic financial institutions in Malaysia. It also provides the *Sharī'ah* committee freedom to ensure sound *Sharī'ah* decision-making.[345]

Several measures have been taken in order to enhance the Islamic Finance Regulatory Framework. These include the amendment on the existing framework to address salient characteristics of Islamic Finance and the setting up of *Sharī'ah* compliance and Governance framework.[346]

The *Sharī'ah* Governance Framework (SGF) is focused on the following areas:

1. *Sharī'ah* Governance Structure: Sets out IFI's *Sharī'ah* governance structures, processes and arrangements to make sure all operations and business activities are in accordance with *Sharī'ah*.[347]

2. *Sharī'ah* Governance Attributes: Provides comprehensive guidance to the Board, *Sharī'ah* Committee and management of IFIs in discharging their duties in matters related to *Sharī'ah*.[348]

3. *Sharī'ah* Compliance and Research Functions: Outlines the functions related to *Sharī'ah* review, *Sharī'ah* audit, *Sharī'ah* risk management and *Sharī'ah* research.[349]

The SGF gets recognition at the international level when one prominent international *Sharī'ah* advisor to the Islamic finance industry, Muhammed Elgari of

345 *Ibid*.
346 Ahmad Hizzad Baharuddin, "The Regulatory Framework of Islamic Financial System in Malaysia," (Director of Islamic Banking and Takaful Department of Bank Negara Malaysia Presentation on 18 April 2011), 14.
347 Bank Negara Malaysia, "*Sharī'ah* Governance Framework," retrieved on 5 November 2011, http://www.bnm.gov.my/guidelines/ 05_*Sharī'ah*/ 02_*Sharī'ah*_Governance_ Framework_ 20101026.pdf.
348 *Ibid.*
349 *Ibid*.

Saudi Arabia, who sits on several *Sharī'ah* committees of such organizations, agrees that Malaysia's *Sharī'ah* Governance Framework for IFIs could become a blueprint for other countries to follow.[350]

4.7 INITIATIVE 6: DEVELOPING THE CENTRE FOR HUMAN CAPITAL DEVELOPMENT IN ISLAMIC FINANCE

To ensure the availability of an Islamic finance talent, Malaysia has placed a strong emphasis on human capital development. Malaysia has done a strategic effort in providing a comprehensive and industry-oriented infrastructure to cultivate a talent pool of skilled professionals.[351]

There are many institutions of Islamic finance education, training and research established in Malaysia with all levels of expertise. Professional courses have been developed to equip Islamic finance knowledge for professional talent, undergraduate and postgraduate students as well as the teaching of research conduct and leadership in Islamic finance and *Sharī'ah*.[352] For the purpose of the development of Islamic finance talent, the Central Bank of Malaysia (Central Bank of Malaysia) has allocated fund amounting to RM 200 million with the key objective to enhance the knowledge, research, talent and intellectual discourse in the field of *Sharī'ah* and Islamic finance.[353]

4.7.1 Islamic Banking and Finance Institute Malaysia (IBFIM)

The Islamic Banking and Finance Institute Malaysia (IBFIM), which shareholders are Central Bank of Malaysia, the Islamic banks and *Takāful* (Islamic insurance) operators, has strategized a framework to develop human talent for the Islamic financial sector. The effort practically succeeded as shown by the number of achievements since its formation in 2001. The institute becomes an important training institute in Islamic finance, handling about 30% of the Islamic finance sector manpower

[350] *Ibid.*
[351] Malaysia International Islamic Financial Centre, "Primer to Islamic Finance," 34.
[352] *Ibid.*
[353] *Ibid.*

annually. Other roles played by IBFIM are to provide total solutions to its clients through a comprehensive range of inter-related services, which include business consultancy and *Sharī'ah* advisory in Islamic banking, *Takāful,* Islamic money and capital markets.[354]

Among the programmes and services offered by IBFIM are as follows:

- Certified Professional Training programmes.
- Continuous Professional Development (CPD) training programmes.
- Customised in-house training programmes .
- Establishment of/or conversion to Islamic financial institutions.
- *Sharī'ah* advisory, *Sharī'ah* audit and stocks screening services.
- *Sharī'ah*-based manuals and process documentation.
- *Sharī'ah* compliance checking for IT and accounting systems.
- Other *Sharī'ah*-based consultancy or advisory services.
- Rare and specialized collections for knowledge and research in the history of money, banking and *Sharī'ah.*
- Publications, translation and sales of Islamic finance books and papers.

4.7.2 International *Sharī'ah* Research Academy for Islamic Finance (ISRA)

The aim of the establishment of the International *Sharī'ah* Research Academy for Islamic Finance (ISRA) is to promote applied research in the area of *Sharī'ah* and Islamic finance. Among other functions of the ISRA is to conduct studies on contemporary issues as well as act as a repository of knowledge for *Sharī'ah* views or

[354] Malaysia International Islamic Financial Centre, "*The MIFC Community Directory: Connecting Business with Islamic Finance*, vol.2, 68.

fatwas. ISRA plays a major role in strengthening human capital development in the areas of *Sharī'ah* through research and dialogue as provided to the practitioners, regulators in both domestic and international arena. Both methods of research and dialogue help ISRA in promoting innovation and dynamism into new boundaries of Islamic finance. With greater research and dialogue, mutual respect and recognition would emerge within the global community.[355]

4.7.3 Securities Industry Development Corporation (SIDC)

The Securities Commission Malaysia (SC) established the training and development institute named as the Securities Industry Development Corporation (SIDC). It functions as a capital market education, training and information resource provider in ASEAN. It was established in 1994 and incorporated in 2007. For more than 15 years, SIDC has been delivering excellence from organizing training programmes for Malaysan and foreign regulators, company directors and market professionals to conducting public investor education seminars on wise investing and investor's rights.[356]

4.7.4 IIUM Institute of Islamic Banking and Finance

In 2005, the International Islamic University of Malaysia established the Institute of Islamic Banking and Finance (IIBF). This institute was supported by the participation of three different faculties, namely the Kulliyyah of Economics and Management Sciences (KENMS), Kulliyyah of Revealed Knowledge (KIRK), and Ahmad Ibrahim Kulliyyah of Law (AIKOL). The involvement of diverse faculties promotes multi-dimensional expertise in the area of Islamic Banking and Finance. This

[355] *Ibid.*, 74.
[356] *Ibid.*, 76.

enables graduates to manage and resolve issues from *Sharī'ah*, Economics, legal, Finance and Management perspectives.[357]

IIiBF offers various study qualifications in Islamic Banking and Finance i.e. Ph.D, Masters, Postgraduate Diploma and Certificate. It also consistently involves in research, product development, consultancy and training, domestically and internationally. IIiBF accepts students from Malaysia and foreign countries.

4.7.5 Islamic Finance Training Centre

Several institutions of higher learning and centres of research and study of all relevant areas of Islamic banking, finance and economics have been established in order to increase the necessary pool of talent for the industry:[358]

- The Islamic Banking and Finance Institute Malaysia (IBFIM) offers technical courses in Islamic banking and finance.

- The International Centre for Leadership in Finance (ICLIF) provides leadership development and management training for financial institutions including Islamic financial institutions.

Other than the above Islamic finance education institutions, six higher learning institutions across Malaysia offer undergraduate and post-graduate programmes in finance. In addition, various programmes have been offered by several learning institutions such Islamic finance training programmes, which aim to develop Islamic finance professionals and to cultivate Islamic finance thought leadership.[359] At the same time, Malaysia has also assisted in developing Islamic finance and educational programmes in tertiary and post-graduate learning institutions in various countries.

---

[357] *Ibid*., 70.
[358] PricewaterhouseCoopers,"*Malaysia, Asia's Islamic Finance Hub*," 59.
[359] Malaysia International Islamic Financial Services (MIFC), "Islamic Finance Talent Programmes," retrieved 10 November 2011, http://www.mifc.com/index.php?ch=seg_tal_pro&pg=seg_tal_pro_ovr&ac=99&ms=2.

With rising demands for more talents in the Islamic finance industry, it is estimated that Malaysia will provide job opportunities for about 12,000 practitioners of Islamic finance a year. Overall, Malaysia has been successful in meeting the domestic industry's demand for talent. Malaysia, with its sharing spirit is now looking to expand its infrastructure and insights into the world to meet the increased global demand for skilled Islamic finance professionals.[360]

4.8 INITIATIVE 7: OTHER REGULATORY AND SHARI'AH SUPPORTIVE BODIES

4.8.1 Labuan FSA's Profile

On 15 February 1996, Malaysia had set up the Labuan Financial Services Authority (Labuan FSA) or formerly known as Labuan Offshore Financial Services Authority (LOFSA). Labuan FSA functions as a single regulatory body to spearhead and coordinate efforts to promote and develop Labuan as an International Business & Financial Centre (IBFC). It indicates the government's commitment to make Labuan a premier IBFC of high repute.[361] Among the roles dedicated to the Labuan FSA is to streamline the government's mechanism in supervising the international business and financial centres and to conduct research and development works as well as to design plans for further improvement and greater efficiency of the Labuan IBFC.[362] The most challenging task for Labuan FSA is to position Labuan as a dynamic financial centre region. To achieve this vision, Labuan FSA embarks a two-pronged plan to develop the Labuan IBFC: by initiating an integrated business and financial centre, which offers a wide range of products and services, including the development of Islamic instruments;

[360] *Ibid.*
[361] Labuan Financial Services Authority, "Corporate Profile," retrieved on 28 October 2011, http://www.lfsa.gov.my/labuan-fsa-s-profile.
[362] *Ibid.*

and by providing a legal framework for the development of industry in Labuan IBFC.[363] With the issuance of the new legislations, it is expected to enhance the competitiveness of Labuan IBFC in the offering of a wider range of financial products and services, including both conventional and Islamic as well as continue to preserve the status of Labuan IBFC as a well-regulated centre.[364]

The following are the amended Acts (As at 2010):

1. Labuan Financial Services Authority Act 1996
2. Labuan Business Activity Tax Act 1990
3. Labuan Companies Act 1990
4. Labuan Trusts Act 1996

New Acts:

1. Labuan Financial Services and Securities Act 2010 (Act 704)

   Note: The following Acts are repealed by Labuan Financial Services and Securities Act 2010 [Act 704]:

   a) Labuan Trust Companies Act 1990 [Act 442]
   b) Offshore Banking Act 1990 [Act 443]
   c) Offshore insurance Act 1990 [Act 444]
   d) Labuan Offshore Securities Industry Act 1998 [Act 579]
2. Labuan Foundations Act 2010 [Act 707]
3. Labuan Islamic Financial Services and Securities Act 2010 [Act 705]
4. Labuan Limited Partnerships and Limited Liability Partnerships Act 2010 [Act 707]

[363] *Ibid*.
[364] *Ibid.*

As a one-stop agency, Labuan FSA is targeting on developing and promoting the growth of the Labuan IBFC. Among others, Labuan FSA is committed to transform Labuan into a full-fledged and premier international financial centre in the world, perhaps second to none in Asia.[365]

4.8.2 International Islamic Financial Market (IIFM)

The primary objective of the establishment of the International Islamic Financial Market (IIFM) as an infrastructure institution is to provide the market mechanism for the advancement and standardization of Islamic financial instruments. Among other roles of IIFM is to provide guidelines and recommendations for the enhancement of Islamic capital and money market globally.[366] Several countries involve in the establishment of IIFM, namely Central Bank of Bahrain, Labuan Financial Services Authority (Malaysia), Bank Indonesia, Central Bank of Sudan, Authority Monetary Brunei Darussalam and the Islamic Development Bank (a multilateral institution based in Saudi Arabia).[367] Other than the founding members, the establishment of IIFM is getting support by its permanent member state bank of Pakistan. The support also comes from Dubai International Financial Centre Authority, ABC Islamic Bank, Bank Islam Malaysia Berhad, European Islamic Investment Bank, Crédit Agricole CIB, National Bank of Kuwait, Kuwait Finance House, Standard Chartered Saadiq as well as other market participants as its members.[368]

4.8.3 Islamic Financial Services Board (IFSB)

In order to provide global prudential standards and guiding principles for industry, the Islamic Financial Services Board (IFSB) has been established as an

---

365 *Ibid.*
366 PricewaterhouseCoopers,"*Malaysia,Asia's Islamic Finance Hub*," 59.
367 International Islamic Financial Market, "IIFM Profile," retrieved on 27 October 2011, http://www.iifm.net/, 27 October 2011.
368 International Islamic Financial Market, "IIFM Profile," retrieved on 27 October 2011, http://www.iifm.net/, 27 October 2011.

international standard-setting organization. The standard includes banking, capital markets and insurance sectors.[369]

Since its inception, the IFSB has issued seven standards:

The guiding principles and technical note for the Islamic financial services industry focusing non-risk management, corporate governance, supervisory review process, capital adequacy, transparency and market discipline, recognition of ratings on *Sharī'ah*-compliant financial instruments as well as the development of Islamic money markets.[370]

4.8.4 Accounting and Auditing Organization for Islamic Finance Institutions (AAOIFI).

The Islamic finance world is auspicious with the establishment of the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) as its contribution towards the issuance of Shari'a standard. The AAOIFI is an Islamic international autonomous non-for-profit corporate body, which its other functions are to prepare accounting, governance, auditing and ethics for Islamic financial institutions and the industry. In order to enhance the industry's human resources and governance structures, the AAOIFI also provides professional qualification programmes (notably Certified Islamic Professional Account (CIPA), the Certified Shari'a Adviser and Auditor (CSAA), and the corporate compliance program).[371]

The AAOIFI was established on 26 February, 1990 in Algiers. The establishment of the AAOIFI is under the Agreement of Association, which was signed by Islamic financial institutions. Then, it was registered on 27 March 1991 in the State of Bahrain. As an independent international organization, the AAOIFI gets substantial

---

[369] PricewaterhouseCoopers,"*Malaysia, Asia's Islamic Finance Hub*," 59.
[370] *Ibid.*
[371] Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), "Overview," retrieved on 28 October 2011, http://www.aaoifi. com/aaoifi/TheOrganization/Overview/tabid/62/language/en-US/Default.aspx.

support from the institutional members consist of (200 members from 45 countries, so far) including Islamic financial institutions, central banks, and other participants from the international Islamic banking and finance industry, worldwide.[372]

Many countries around the world have given encouraging support for the implementation of the AAOIFI Standards with all of them adopted the standard in their countries, namely the Kingdom of Bahrain, Jordan, Lebanon, Sudan, Qatar, Syria and Dubai International Financial Centre. In other countries such as Australia, Indonesia, Malaysia, Pakistan, Kingdom of Saudi Arabia, and South Africa, the authorities have issued guidelines based on the AAOIFI's standards and pronouncements.[373]

4.9 ISLAMIC FINANCE PERFORMANCE IN MALAYSIA

In Malaysia, the liberalization in the Islamic banking market started with the opening of the first foreign Islamic bank in August 2005.[374] The structure of Malaysia Islamic banking business has changed as a result of the conversion of Islamic banking windows into subsidiaries in 2007, which reflected to the increasing domestic focus on Islamic banking business. This conversion contributed to clearer accountabilities under separate board and management structures.[375]

As of 2011, the number of Islamic bank in Malaysia achieved 17 full-fledged Islamic banks where six of them are foreign-owned banks. They are the Kuwait Finance House (Malaysia) Bhd, Standard Chartered Saadiq Berhad, HSBC Amanah Malaysia Berhad, Al Rajhi Banking & Investment Corporation (Malaysia), OCBC Al-Amin Bank Berhad and Asian Finance Bank Berhad.[376]

---

[372] *Ibid.*
[373] *Ibid.*
[374] Foreign and local Islamic banks are licensed under the Islamic Banking Act 1983.
[375] PricewaterhouseCoopers,"*Malaysia, Asia's Islamic Finance Hub*," 59.
[376] Bank Negara Malaysia, http://www.bnm.gov.my/, 8 October 2011.

Islamic banking assets in Malaysia show a significant growth in the first seven months of 2011 with the increase of 15 percent to 389.3 billion Ringgit ($123 billion). The increase has strengthened the country's position as the global hub for Islamic finance.[377]

According to the report issued by Malaysia's ministry of Finance 2011-2012, Islamic asset climbed to 21 percent of Malaysia's total banking in July from the same period a year earlier. The Islamic financing sector increased 17 percent to 246.8 billion Ringgit and represented 23 percent of total financing, while a deposit's sector grew 14 percent to 299.1 billion Ringgit.[378]

Syarikat *Takāful* Malaysia was established in 1984 under the *Takāful* Act 1982. The company has made a significant growth since its inception and constantly served Malaysian with Islamic principle's protection. In 2007, Malaysia *Takāful* fund's asset achieved US$3 billion (RM 9 billion) or 7% of the total assets of the insurance and *Takāful* industry in Malaysia. The number of *Takāful* operators in Malaysia increased from two to eight *Takāful* companies with a contribution worth US$0.8 billion in 2007.

Malaysia has become the world largest *Takāful* assets in 2009 with the total of *Takāful* assets worth US$3.2 billion, which dominated 26 percent of the total global *Takāful* assets around the world. This achievement resulted from the growth *Takāful* demand in Malaysia, with a compound average of 27% of net contribution between 2005 and 2010 that shows the increase in *Takāful* coverage as the preferred option.[379]

Based on a Bloomberg report dated 7 October 2011, Malaysian *Takāful* assets rose 17 percent to 16.3 billion ringgit as at the end of July from the same period in 2010.[380]

377 Bloomberg Business News, "Malaysian Islamic Banking Asset Rise 15% to 123 Billion," retrieved on 7 October 2011, http://www.bloomberg.com/news/2011-10-07/malaysian-islamic-banking-assets-rise-15-percent-to-123-billion.html.

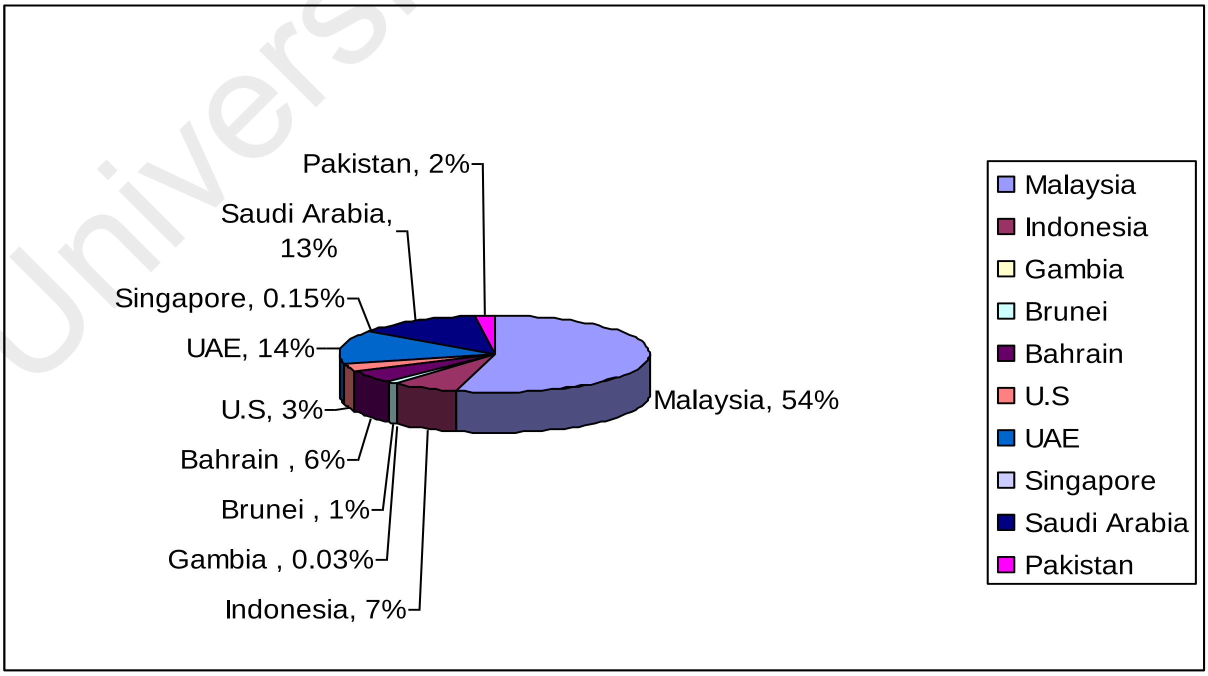
378 *Ibid.*

379 *Ibid.*

380 Bloomberg Business News, "Malaysian Islamic Banking Asset Rise 15% to 123 Billion," retrieved on 7 October 2011, http://www.bloomberg.com/news/2011-10-07/malaysian-islamic-banking assets-rise-15-percent-to-123-billion.html.

In the *Sukuk* sector, Malaysia has recorded a double *Sukuk* issuance in the year 2009, when the market faltered because of the fallout from the global financial crisis due to some comments made by Sharia scholars about the Sharia compliance of *Sukuk* that had already been issued. Malaysia has issued a total of 65 *Sukuk* in 2009, which representing approximately 48% of the world *Sukuk* issuance that shows the country's depth in the *Sukuk* market. The Malaysian government has formed a great formula in the Islamic finance development - from the establishment of the Malaysian International Islamic Finance Centre to position the country as a global leader in Islamic finance and to the exemption of various taxes towards Islamic banks, *Takāful*, brokerages and offshore *Sukuk* investors. These great measures have encouraged government-related entities (GREs) and corporates to get involves in the domestic market. The *Sukuk* issuance in Malaysia involved large corporates such as Sime Darby (not rated) and Petroliam Nasional Bhd. (Petronas, A-/Stable/--), as well as prominent GREs such as Terengganu Investment Authority (not rated), and Cagamas (not rated).[381]

Chart 4.1: *Sukuk* Issuance by Country 2009:



Data of Dec.31, 2009. Sources: Standard & Poor's, Zawya

[381] Standard and Poor's Rating Services, *Islamic Finance Outlook 2010*, (McGraw Hill, 2010), 16.

©Standard and Poor's 2010.

As reported by Bloomberg on 7 October 2011,"Malaysian Islamic capital market now exceeds $1 trillion and is growing as rapidly as the conventional capital market[382]." The Southeast Asian market, consists of about 60 percent Muslim population from 27 million people, has relaxed foreign ownership rules for Islamic institutions to attract investment and stimulus growth large market for *Sharī'ah*-compliant bonds or *Sukuk*. The nation has $112.3 billion of debt outstanding representing 62.7 percent of the world's total, the ministry said. According to the data compiled by Bloomberg, global sales of *Sukuk*, climbed to $18 billion in 2011, from $11.8 billion in the same period of 2010.[383]

Malaysia has successfully attracted foreign investors to issue *Sukuk* using its capital market base. According to the report by MENAFN.com dated 10 October 2011, the Kuveyt Turk Participation Bank (KPTB), which is in majority owned by Kuwait Finance House, launched its *Sukuk al-Ijara* issuance with a five-year period worth $350 million. The important thing is that the roadshow began in Kuala Lumpur, Malaysia, which indicated the issuers from the Middle East, largely from the Gulf Co-Operation Council (GCC) and now Turkey for the first time, were changing position to investors in Malaysia and Asia to raise their funding requirements. From Malaysia, the roadshow moved to other Asian markets, and then proceed to the Middle East and Europe on October 18, 2011.[384]

In the meantime, the Abu Dhabi National Energy Company is in progress to launch a RM3.5 billion *Sukuk* programme in Malaysia to vary their funding sources. In a statement to the Abu Dhabi Securities Exchange, the company confirmed the issuance programme, and insisted that subject to the regulatory approval obtained from the

---

[382] Bloomberg Business News, "Malaysian Islamic Banking Asset Rise 15% to 123 Billion," retrieved on 7 October 2011, http://www.bloomberg.com/news/2011-10-07/malaysian-islamic- banking-assets-rise-15-percent-to-123-billion.html.

[383] *Ibid*.

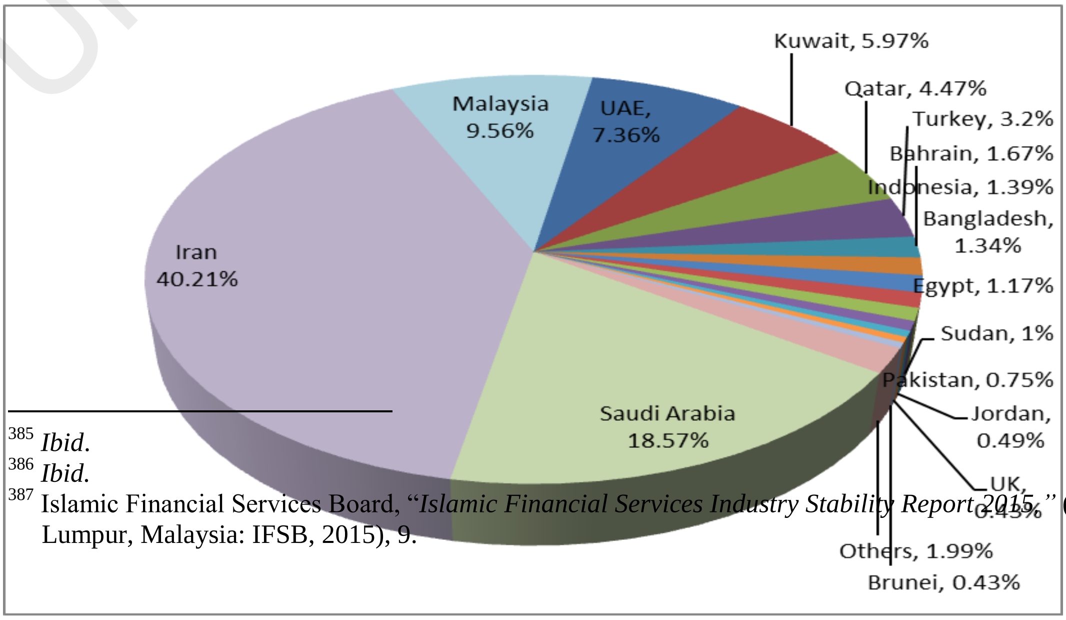
[384] Arab News Website, "Bond Issuers Turn to Malaysia, Asia," retrieved on 10 October 2011, http://www.arabnews.com/node/394028.

Securities Commission of Malaysia, it aims to issue a first tranche under the programme "quickly if and when market conditions are optimal."[385]

Based on the record, there are several foreign issuers that have originated *Sukuk* in Malaysia including the World Bank and its private sector funding arm, namely the International Finance Corporation (IFC); the $100 million *Sukuk Al-Ijārah* issued by Japan's Nomura Holdings; the RM500 million 10-year *Sukuk* issued by the National Bank of Abu Dhabi and the RM100 million *Sukuk Al-Ijārah* issued by the Islamic Development Bank.[386]

The biggest potential breakthrough occurs in 2010 when the Saudi Arabia's Al-Rajhi Bank in collaboration with Cagamas Berhad (the National Mortgage Corporation of Malaysia) and a leading securitization house, joint together in issuing *Sukuk al-Amānah Li Al-Istithmār (Sukuk ALim)*, which was the underlying structure for Cagamas's RM 5-billion Islamic Commercial Paper (ICP) and Islamic Medium Term Note (IMTN) programme. This innovative structure of *Sukuk* and the "first-of-its-kind," was sold to investors in Saudi Arabia and became Al-Rajhi's manifestation of a newly found strategy in bridging the gap and to facilitate cross-border activities in the Islamic capital market between Malaysia and the Middle East.

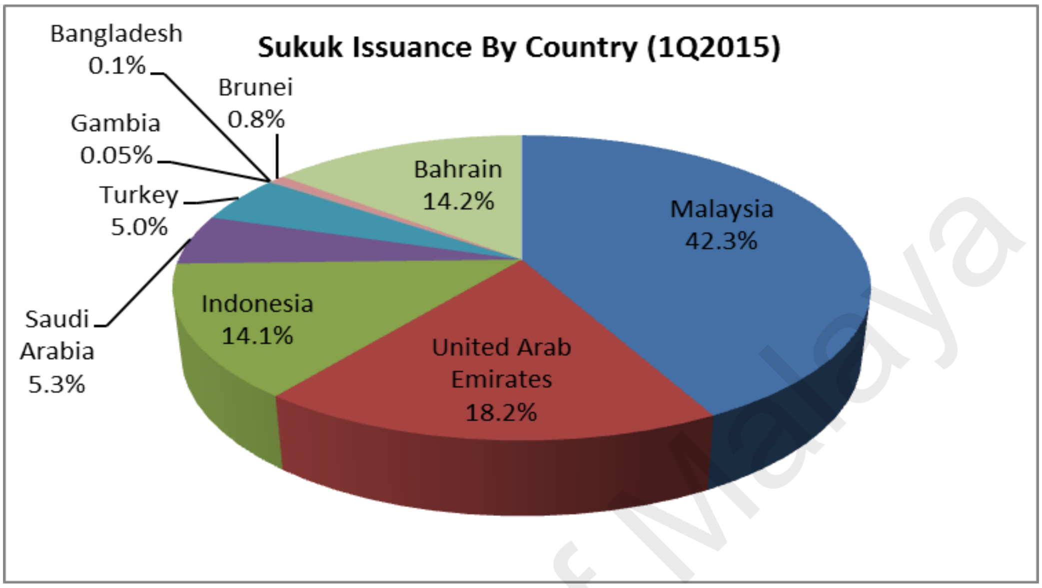
Chart 4.2: Shares of Global Islamic Banking Asset 2014.[387]



385 *Ibid*.
386 *Ibid*.
387 Islamic Financial Services Board, "*Islamic Financial Services Industry Stability Report 2015*," (Kuala Lumpur, Malaysia: IFSB, 2015), 9.

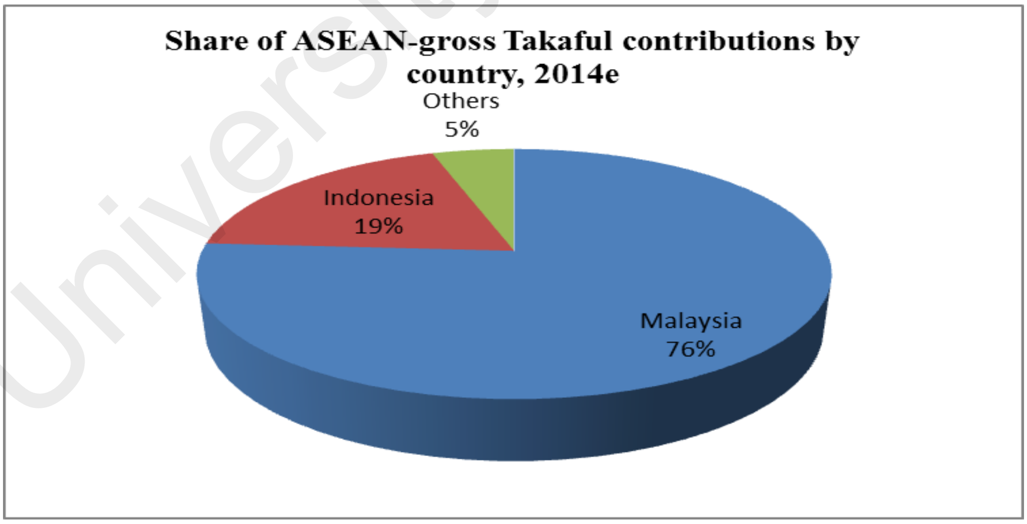
Source: Regulatory authorities, Bloomberg, Zawya,central banks, Individual institutions, corporate communications, The Banker, KFHR

Chart 4.3: Global Sukuk Issuance by Country (1Q22015)[388]



Source: Bank Negara Malaysia, 2015.

Chart 4.4: Global Takaful: Share of ASEAN-Gross Takaful contributions by Country, 2014e.[389]

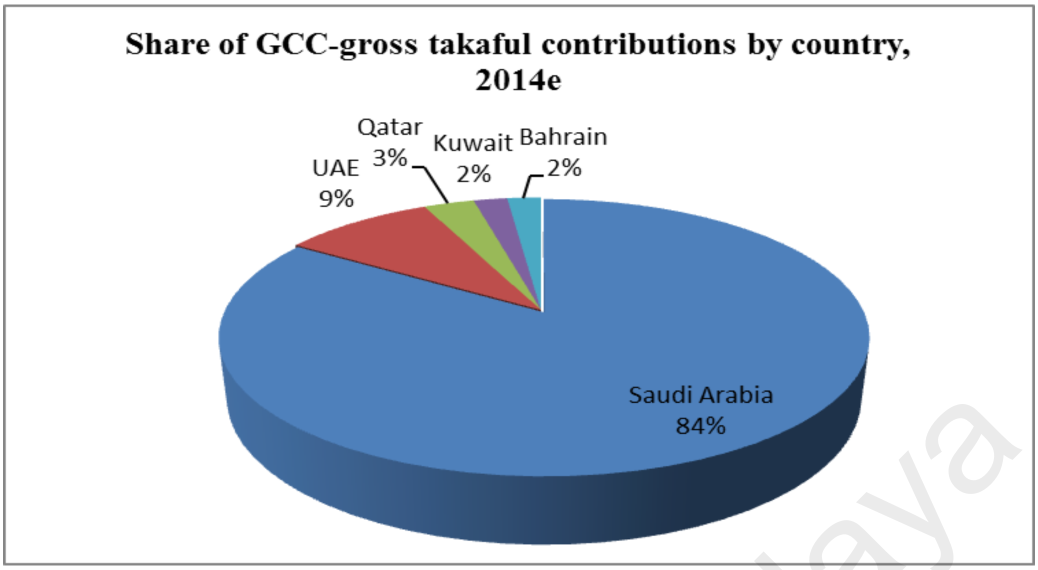


Source: Malaysia Takaful Association and Ernst & Young, 2015.

[388] Bank Negara Malaysia, "*Global Sukuk Report 1Q2015*," (Kuala Lumpur, Malaysia: Bank Negara Malaysia), 3.

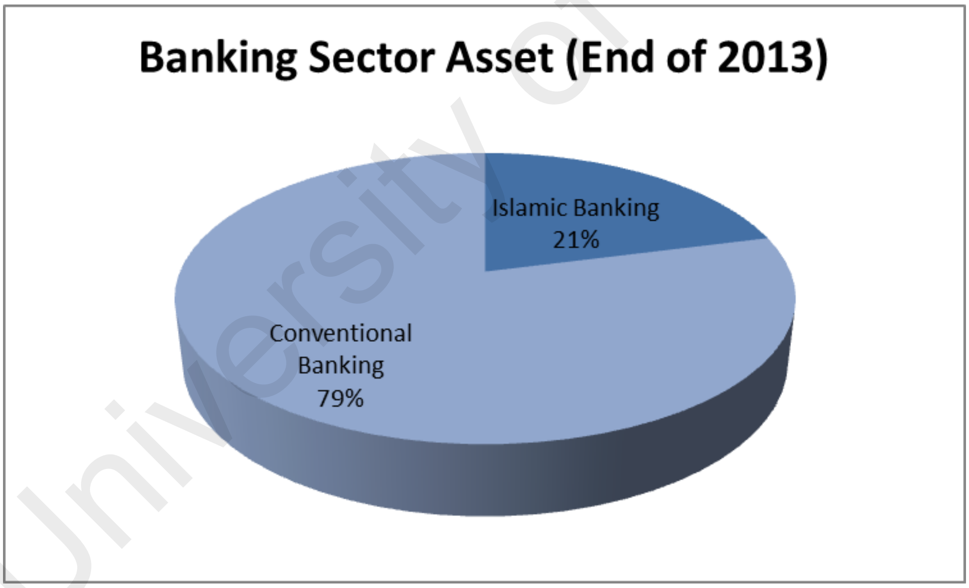
[389] Malaysia Takaful Association and Ernst & Young,"*Malaysian Takaful Dynamics, Central Compendium 2015*," (Kuala Lumpur, Malaysia: Malaysia Takaful Association and Ernst & Young, 2015), 15.

Chart 4.5: Global Takaful: Share of GCC-Gross Takaful contributions by Country, 2014e.[390]



Source: Malaysia Takaful Association and Ernst & Young, 2015

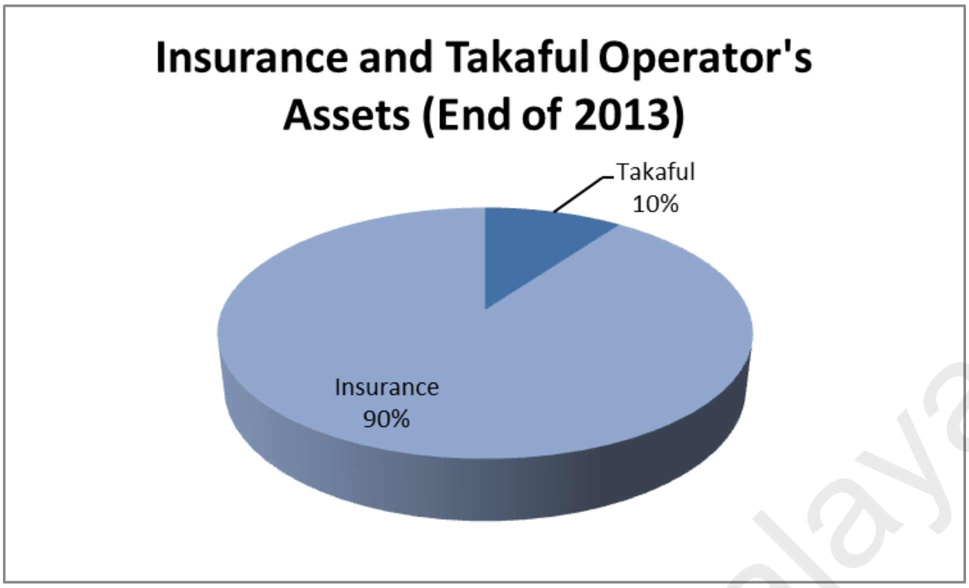
Chart 4.6: Malaysia Islamic Banking Asset (End 2013)[391]



Source: CIMB ISLAMIC, 2015.

[390] *Ibid.*
[391] CIMB ISLAMIC, *"Malaysia Islamic Finance Report 2015,"* (Kuala Lumpur, Malaysia: CIMB ISLAMIC, 2015), 149.

Chart 4.7: Malaysia Insurance and Takaful Operator's Assets (End of 2013)



Source: CIMB ISLAMIC, 2015

Table 4.4: Malaysia's Performance indicator among other countries[392]

IFDI INDICATOR		
	COUNTRY	INDICATOR VALUE
1	**MALAYSIA**	**93**
2	BAHRAIN	76
3	OMAN	64
4	UAE	57
5	QATAR	40

QUANTITATIVE DEVELOPMENT INDICATOR		
	COUNTRY	INDICATOR VALUE
1	**MALAYSIA**	**75**
2	SAUDI ARABIA	45
3	UAE	37
4	QATAR	36
5	KUWAIT	35

KNOWLEDGE INDICATOR		
	COUNTRY	INDICATOR VALUE
1	**MALAYSIA**	**140**
2	BAHRAIN	62
3	JORDAN	53
4	PAKISTAN	49
5	UAE	38

GOVERNANCE INDICATOR		
	COUNTRY	INDICATOR VALUE
1	BAHRAIN	90
2	**MALAYSIA**	**82**
3	PAKISTAN	67
4	KUWAIT	65
5	SUDAN	59

CORPORATE SOCIAL RESPONSIBILITY INDICATOR		
	COUNTRY	INDICATOR VALUE
1	OMAN	85
2	BAHRAIN	76

[392] *Ibid.*, 285.

3	JORDAN	73
4	UAE	57
5	INDONESIA	48
6	BANGLADESH	47
7	BRUNEI DARUSSALAM	43
8	**MALAYSIA**	**40**

AWARENESS INDICATOR		
	COUNTRY	**INDICATOR VALUE**
1	OMAN	156
2	**MALAYSIA**	**130**
3	BAHRAIN	127
4	UAE	103
5	QATAR	71

4.10 ISLAMIC FINANCIAL HUB GLOBAL RACE

There is a global race among Islamic finance countries to become an Islamic finance global hub. The vying involves not only the well-known Islamic finance country, but also a smaller country targeting the same objective. Islamic banking is now burgeoning in the global economic scenario. Subsequently, it forms part of the equation in international finance, whether at a government-to-government or the private sector levels. Its acceptance has grown over the years and has now existed in over 60 countries.[393] As Islamic finance has become a part of the global financial system, many countries are investing a lot in positioning themselves as Islamic financial global hubs, including the established financial centres such as London, Hong Kong, Malaysia and GCC countries.

Obviously, the growth of Islamic finance has no indication to slow down, is quite the reverse. As reported by Mckinsey & Company in 2007, by the year 2010, assets held by the world Islamic banking community will reach the $1tn mark. Meanwhile, the forecast in the insurance sector by Swiss Re suggests that by 2015, it will have risen to $3.3 bn (up from $650m in 2005) in *Takāful* premiums in the MENA (Middle east and North African) region. In the same period, Malaysian premiums expand from $395m to $1.23 bn and over. In other countries, the *Takāful* premiums

[393] PriceaterhouseCoopers, "Islamic Finance in Malaysia," tetrieved on 25 September 2011, http://www.pwc.com/my/en/issues/islamic-finance-malaysia.jhtml.

reach \$1.2 bn in Indonesia by 2015, \$851m in the US, \$269m in the UK, \$173m in Africa and \$18m in Turkey, based on the Swiss re-projection report.[394]

The future of Islamic finance is somehow bright as the global report suggests that there are other incentives for exploring *Sharī'ah*-compliant alternatives where the Gulf investors found that more money can be made in Islamic banking compared to the conventional counterparts given (that) the regulatory regimes in the Islamic banking industry are still developing. The expansion and internationalization of the Islamic finance industry has come from the banking community itself. Although over the last two decades the scores of new Islamic banks have sprung up in a wide range of Muslim-majority countries, the growth potential of the industry has not been lost on the multinational players. Size is vital because as Fitch explained, 'bigger banks, in general, receive higher ratings than small banks because they have a greater capacity to absorb financial problems.[395]

Countries around the world are setting their utmost target for the Islamic finance industry as Islamic finance global hubs as part of their highest achievement. For instance, the UK government has lined up a plan to position the UK as the global gateway for Islamic finance and the task was dedicated to the UK Treasury to undergo a feasibility study to evaluate the UK government's potential and possibility to become as issuer of *Sukuk*s. The fact that the UK government is keen on promoting London as a centre for Islamic finance is most ideally due to the creation of business opportunities for the city as well as to show the British Muslim community of the government's acceptance of the Islamic financial system and that there is no obstacle towards Muslim's customers to choose this financial system.[396]

---

[394] Swiss Re Sigma Study 2003: Axco Global Statistics 2005. Quoted in 'Issues in Islamic Finance and (re) Takaful,' PricewaterhouseCoopers.

[395] Nesrine Jeffer, *Islamic Wealth Management: A Catalyst for Global Change and Innovation*, 78.

[396] Rodney Wilson,"The Development of Islamic finance in the UK," (Working Paper, Kuwait Programme on Development, Governance and Globalisation the Gulf States, 2009), 2.

At the same time, the Islamic finance system also received approval from the Singapore government, which starts to give more attention to Islamic finance in recent years. The Monetary Authority of Singapore (MAS) on June 2006 gave its consent to banks to be involved in non-financial activities such as commodity trading to facilitate *Murābahah* transactions for clients' investments. Prior to this consent, there is no approval for the banks to exercise non-financial activities such as trading; which situation is unusual in the banking and finance practice. This measure indicates MAS's recognition on the fundamental characteristics of *Murābahah* - a key form of Islamic financing in the Middle East.[397]

MAS involvement in Islamic finance is obvious by the joining of IFSB as an observer member in December 2003 and MAS became a full member in April 2005. Currently, MAS is actively participating in other Islamic finance activities such as Islamic Money Market Taskforce, the Supervisory Review Process Working Group and the Special Issues in Capital Adequacy Working Group.[398] In 2005, Singapore has taken a significant measure by waiving the imposition of double stamp duties in Islamic transactions comprising real estate and accorded the same concessionary tax treatment on income from Islamic bonds that are applicable to conventional bonds. In July 2001, Maybank Malaysia started its business in Singapore. They encapsulated their service with Islamic banking through the introduction of the Singapore Unit Trusts Ethical Growth Fund that complies with the principles of the *Sharī'ah*.[399] Further, in November 2005, the bank announced the *Sharī'ah*-compliant online savings account and *Sharī'ah*-compliant savings cum checking account.[400]

[397] Asmani, A., "Banks Get Green Light to Offer Another Islamic Product", *The Straits Times (Singapore)*, 13 June 2006.
[398] Monetary Authority of Singapore (MAS) Report 2006/2007 (2007), Monetary Authority of Singapore, Singapore, 53.
[399] Habibullah Khan & Omar K.M.R. Bashar, "Islamic Finance: Growth and Prospects in Singapore," (U21 Global Working Paper Series, No. 001/2008), 4.
[400] Siow, L. S. , "Maybank Launches Islamic Banking", *The Business Times (Singapore)*, 26 November 2005.

In term of size, Singapore domestic market is quite small and there is no sufficient awareness on Islamic finane. The fact is, in the region, Malaysia is a leading Islamic industry. However, Singapore has a good prospect for positioning itself in a niche market. For instance, as of 2006 there were nearly 227 million Muslims in Southeast Asia, which is about 40 percent of the total population in the region. Being a regional financial hub, Singapore could target a big pie of this Muslim community since Islamic finance in Southeast Asia is not as far advanced as in the Middle East despite the strong growth potential.[401] Hong Kong has established its *Sharī'ah* Advisory Council and in Indonesia, the Central Bank is stimulating Islamic banks to intensify efforts to reach $10 billion in assets by 2008. These international financial centres are focusing their efforts on the fast track growth of *Sukuk*s linked to mega infrastructure and real estate projects and the advent of wealth management services, including asset management.[402]

In comparison to the financial centre's size, Hong Kong is in the third place as the largest financial centre after New York and London and now looking forward to becoming the gateway for Islamic finance to cater for opportunities in mainland China as well as other countries in the region such as Korea, Taiwan, Vietnam, Laos and Cambodia.[403] In order to diversify the Hong Kong's financial services offerings, the government of Hong Kong set to becoming as an Islamic finance hub, especially for capital market's instruments and investments.[404] In fact, the Hong Kong Administration has done brilliant idea by exercising tax neutrality measures to facilitate the development of Islamic finance. These measures seek to approach disadvantageous

---

[401] Habibullah Khan & Omar K.M.R. Bashar (2008), "Islamic Finance: Growth and Prospects in Singapore," 6.

[402] Nesrine Jeffer,, *Islamic Wealth Management: A Catalyst for Global Change and Innovation*, 67-68.

[403] Arab News, "Hong kong Eyes Islamic Finance Product," retrieved on 5 October 2011, www.arabnews.com/node/321247%3Fquicktabs_stat2%3D0+&cd=1&hl=en&ct=clnk&gl=myhttp://archive.arabnews.com/.

[404] *Ibid.*.

treatments on the issuance and transactions of *Sukuk* vis-à-vis conventional bonds. They will enhance the commercial viability of *Sukuk* in the market."[405]

Hong Kong enjoys several specialties, which made the island suitable as an Islamic finance hub. Hong Kong's advantages lie in its strategic location, highly developed financial markets and infrastructure, and a business-friendly free-market environment.[406]

However, there is a challenge facing Hong Kong in developing Islamic finance. The fact is that the Islamic community in Hong Kong is not big. Hence, in terms of local market, it will not support Hong Kong's domestic Islamic finance to grow. As Mr Eddie Yue, Deputy Chief Executive of the Hong Kong Monetary Authority and Executive board Chairman of the Treasury Markets Association, stressed that there is no intention for Hong Kong's authority to position the country as a market that can match the supply and demand of Islamic products from the domestic angle.[407]

In the Africa region, Sudan, a Muslim country located in the central Africa, is among the most famous Islamic finance countries as Sudan practices Islamic finance in its entire financial system. However, to a certain situation, this decision causes the Sudan's Islamic banks to remain small due to the limited size of its economy.

In Gulf Countries, the value of *Sharī'ah*-compliant assets is impressive. Total assets in GCC are worth over US$262 billion when the figures for Saudi Arabia, Bahrain, Qatar, Kuwait and the Unites Arab Emirates are aggregated, compared with $235.3 billion in the Islamic Republic of Iran. As the total of *Sharī'ah*-compliant assets worldwide amounted to around $640 billion at the end of 2007, this implies that the GCC countries accounted for around 41 percent of the total. Furthermore, the assets

---

[405] *Ibid.*

[406] Eddie Yue, "Hong Kong's Possible Role in Islamic Finance," (Welcome address by Deputy Chief Executive of the Hong Kong Monetary Authority and Executive Board Chairman of the Treasury Markets Association, at the Hong Kong Showcase on Islamic Finance, Dubai and Amman, 11-12 May 2008), 3.

[407] *Ibid.*

have been growing rapidly as table 4.4 shows due to the hike of oil and gas prices in 2007, which fed through to government spending in the GCC and consequently, a buoyant level of economy activity.[408]

Table 4.5: *Sharī'ah*-Compliant Financial Assets by Country

Rank	Country	Assets (US$ billion)	Growth, 2007 (%)
1	Iran	235.3	27.5
2	Saudi Arabia	92.0	26.1
3.	Malaysia	67.1	32.3
4.	Kuwait	63.1	44.3
5.	United Arab Emirates	49.1	35.9
6.	Bahrain	37.4	42.8
7.	Qatar	21.0	77.5
8.	United Kingdom	18.1	60.7
9.	Turkey	15.8	65.5
10	Pakistan	6.3	39.0

Source: The Banker, Supplement on the Top 500 Islamic Financial Institutions, October 2008.p.24. The data refers to December 2007.

Islamic financial institutions in GCC have successfully performed well in its business with profits and rates of return much higher than in Iran's state-owned Islamic banks. As shown in Table 4.5, Al Rajhi Bank led others in term of the most profitable Islamic financial institution, partly generated from the high margins between its minimal costs of funding and the rates charged for its financing. However, in comparison to the total Islamic finance asset, six of the ten largest Islamic finance companies around the world are from Iran. Despite US sanction against Iran, the growths of Islamic finance are quite encouraging and most probably better performance if the sanction could be eliminated. This fact is due to the large customer base in Iran if compared to the GCC, reflecting its population size of over 70 million. However, because of its relative economic and financial isolation, it has been largely cut off from international developments in Islamic finance. The GCC countries are more open in

[408] Rodney Wilson,"The Development of Islamic finance in the UK," 1.

terms of financial policy. In Dubai, local Islamic financial institutions operate with the presence of a foreign Iranian Islamic financial institution.[409]

Table 4.6: Top 10 Commercial Banks ranked by ROA (only Filly Sharia compliant banks with minimum $100m in profit)[410]

Rank	Institution	Country	Pre-Tax Profits (US$ million)	ROA (%)
1	Pasargad Bank	Iran	663	3.40
2	Karafarin Bank	Iran	170	3.30
3	Sina Bank	Iran	203	3.27
4	Masraf al-Rayan (Al Rayan Bank)	Qatar	554	2.75
5	Faisal Islamic bank of Egypt	Egypt	179	2.64
6	Bank Rakyat (bank Kerjasama Rakyat Malaysia Berhad)	Malaysia	613	2.41
7	Bank Islam Brunei Darussalam Berhad (BIBD)	Brunei	121	2.41
8	Dubai Islamic Bank	UAE	786	2.38
9	Al-Rajhi Bank	Saudi Arabia	1823	2.33
10	Qatar International Islamic Bank Doha	Qatar	226	2.26

Source: The Banker November 2015 Special Report, "*Top Islamic Financial Institutions,"* 2015.

Among the issues raised in GCC's *Sharī'ah* governance are the different of *Sharī'ah* deliberation by various *Sharī'ah* boards of Islamic finance institution. In the GCC, the Islamic banks, through their *Sharī'ah* boards play roles in issuing deliberations rather than the central body of *Sharī'ah* Advisory as normally practiced in other countries such as Malaysia. The members of *Sharī'ah* boards are specialists in Fiqh Muamalat– the branch of Islamic jurisprudence that is concerned with civil contracts, including those governing financial transactions are appointed in the board to provide advice on the financial products offered. The system of *Sharī'ah* board in monitoring the compliance of *Sharī'ah* has worked well as the members of the boards behave in a constructive manner rather than restrictive and have been quite willing to

[409] *Ibid.*
[410] The Banker November 2015 Special Report, "*Top Islamic Financial Institutions*," (London, United Kingdom: Financial Times Ltd.), 3.

approve new types of deposit and finance facilities. This system has indeed become market-driven, which has resulted in product differentiation and extended customer choice.[411]

In the U.A.E, there is an effort to establish a higher *Sharī'ah* Council, which functions to control and supervise the existing six Islamic banks now operating throughout the country.[412] This kind of approach is similar to the Malaysian system where the national boards issue fatwa to all banks while the internal bank's *Sharī'ah* boards propose the *Sharī'ah* views with regard to the National board approval. In the situation where the national *Sharī'ah* authorities are absence, the boards of each financial institution can issue their own fatwa.[413]

The conflict in different fatwas between *Sharī'ah* boards are inevitable as each board preserves its power to make independent pronouncements.[414] There are widespread discussions regarding to the shortage of suitable *Sharī'ah* candidates to join as a member of *Sharī'ah* board, with some serving many institutions, also raising issues about the time they can dedicate to the work for each board.[415] Malaysia has implemented a control on their consultant's engagement in institutions where a consultant can serve only in one board of banking institution and another board in *Takāful* companies. In contrast to GCC countries, there are no restrictions imposed by the regulators towards *Sharī'ah* consultants where they are free to join any institutions without limitation. However, the argument is raised on how far the accountability of the *Sharī'ah* boards in managing their time in approving the proposal of products from various Islamic finance institutions. There are pros and cons on this issue. Some views that the consultant with many consultations will benefit the Islamic finance institutions as the consultant is a prominent scholar who is rarely available. On the other hand, this

---

[411] *Ibid.*
[412] *Ibid.*
[413] *Ibid*
[414] *Ibid.*
[415] *Ibid.*

method of consultation is considered as a monopoly where it closes chances to other consultants who are also scholars in Islamic banking and finance. Based on this argument, the Kuala Lumpur-based Islamic Financial Services Board (IFSB), which functions to advise central banks on the regulation of Islamic financial institutions, has initiated an effort in issuing guidelines on *Sharī'ah* governance in July 2009. This effort has been supported by all GCC members except Oman that is involved with the work of the IFSB. However, this guideline is not a mandatory to be implemented throughout the region.

For instance, although Islamic finance in Saudi Arabia shows a significant growth, its legal framework is still lagging. There is no dedicated Islamic banking law in Saudi Arabia as well as its mortgage law that has been pending for the last three years and is still not adopted. Affected by this legal mismanagement are both the banks and customers when the banks fail to adopt a constructive legal framework for the introduction of various Islamic finance products.[416]

Perhaps, the GCC countries prefer the privatization concept rather than the nationalization one.[417] However, a recent issue on *tawarruq* shows the mis-deliberation by the GCC jurists when they initially passed a *tawarruq* contract as *Sharī'ah*-compliant, but later, became non-*Sharī'ah*-compliant due to the comment made by the Islamic finance prominent scholar, Syeikh Taqi Usmani (Chairman of AAOFI) who views that *Tawarruq* contract is tandem to riba. The issue remains unresolved or replaced by another compliant contract, although has been reviewed by scholars. The verification of *Sharī'ah*, however, should not harm and prevent innovation in Islamic finance. Thus, the right way to move forward is through a mutual recognition of the interpretations and decision of *Sharī'ah* principles approved by recognized *Sharī'ah* bodies around the world.

[416] Arab News, Mushtak Parker: "Malaysia pushing for Islamic Finance Legal Framework," http://arabnews.com/economy/islamicfinance/article208977.ece., 12 September 2011.
[417] Rodney Wilson,"The Development of Islamic finance in the UK," 9.

It is important to admit the role of financial institutions in the GCC as significant sources of capital and contributing towards the development of Islamic finance worldwide, especially in Asia. The strategic location of GCC at the heart of the Muslim supports the region to serve an Islamic finance hub, linking Europe, Asia and Africa. The establishment of the GCC-based Islamic banks around the world indicates the starting point of the vision.[418] Moving forward, the GCC countries like Qatar and Dubai have established free zones financial centres governed by their own laws and regulations based on the English common law, which applies to finance. The Qatar Financial Centre and the Dubai International Financial centres (DIFC) are using separate jurisdictions from the outside civil and *Sharī'ah* regulations, where the local *Sharī'ah* court remits being largely confined to disputes within families over matters such as inheritance.[419]

However, the 2008 credit crunch issue occurred in Dubai has made the reputation of Islamic banks in the country disputable. This issue is among the challenges faced by the Islamic banking sector in Dubai, where the corruption was revealed to involve the former Dubai Bank employees with the local property finance company, al-Tamweel. Al-Tamweel has seen its share price slashed on the Dubai Financial Market, with a fall from AED 8.25 in January to AED 2.44 by October.[420]

In the progress of Islamic finance towards the era of financial centre, Malaysia has also played an important role in positioning the country as a global hub for Islamic finance. As an effort to retain Malaysia as a leading country in Islamic finance, the government announced a number of measures. The measure included tax exemption policy for 10 years for Islamic banks licensed under the 1983 Islamic banking act on income derived from *Sharī'ah*-compliant banking business using international

---

418 *Ibid.*, 30.
419 *Ibid*.
420 *Ibid.*

currencies. The same policy was also implemented on the business based on *Sharī'ah* principles conducted by local and foreign companies managing funds of foreign investors approved by the Securities Commission.

This tax exemption policy is expected to attract fund managers to establish operations in Malaysia, especially for managing funds based on *Sharī'ah* principles as reported by the PricewaterhouseCoopers analysis. The model of tax exemption could be illustrated from the set-up of reputable fund managers to the creation of more *Sharī'ah* funds and products and then will be marketed to foreign investors. This situation resulted in the formation of Malaysia as the hub and thus, attracted *Sharī'ah* monies for reinvestment around the region.

Malaysia's central bank, Central Bank of Malaysia, plays vital roles in positioning the country as a global hub for Islamic banking and finance. With the support from Malaysia's government through tax redemption policy, the Central Bank of Malaysia also plays vital roles in structuring a sound Islamic finance regulation comprises the Islamic banking, Islamic Capital Market and *Takāful* industry. In terms of human resource development, Central Bank of Malaysia again took an effort in establishing the International Centre for Education in Islamic Finance (INCEIF) and International Shari'ah Research Academy for Islamic Finance (ISRA) to provide training and conduct research in Islamic finance. Based on the previous record, Malaysia has successfully developed its Islamic finance sector, comprises the Islamic banking as well as *Takāful* and Islamic Capital Market, and is leading other countries in Islamic finance.

Malaysia, in the past 30 years, has developed its Islamic financial system with several reformation programmes through legislation, tax breaks and indirect subsidies; all of these must be viewed as an aggressive and affirmative action in positioning the country as a global hub for Islamic finance. According to the report released on 7th

October 2011, Malaysia's Islamic banking assets rose 15 percent to 389.3 billion ringgit ($123 billion) in the first seven months of 2011, strengthening the country's position as the global hub for *Sharī'ah*-compliant financing.[421] The Islamic capital market now exceeds $1 trillion and is growing as rapidly as the conventional capital market.[422] According to the report, the Islamic insurance or *Takāful* assets rose 17 percent to 16.3 billion ringgit at the end of July from the same period last year. The sector accounted for 8.7 percent of Malaysia's total insurance industry as of July 31, from 8.3 percent a year earlier.[423]

However, continuous efforts still have to be maintained by all parties involved such as the government, Islamic finance institution, scholars and public in supporting the Islamic finance development to further position the country as a global hub for Islamic finance. Indeed, in the end, the global hub competition indeed will not only be won by one ultimate country, but there will be many. After all, the competition is good for the Islamic finance development. Regardless who is competing, the winner will be the Islamic finance itself and above all its customers. A higher network coverage and competition means lower prices, more products and better services.

4.11 CHAPTER SUMMARY

Based on the review across nations, a conclusion from the Islamic finance movement worldwide shows an indication of each country's intention to become a leader in Islamic banking and finance. For instance, Singapore aims at being an Islamic capital market hub, Dubai is willing to be an Islamic finance hub, Bahrain emerges as an Islamic investment banking hub, and Malaysia is making a significant effort in

---

[421] Business Week, "Malaysian Islamic Banking Assets Rise 15% to $123 Billion," retrieved on 7 October 2011, http://www.businessweek.com/news/2011-10-07/malaysian-islamic-banking-assets-rise-15 percent- to-123-billion.html.
[422] *Ibid.*
[423] *Ibid.*

positioning itself as a global hub for Islamic finance. This seems to be something really big as the global Islamic financial hub is about international cities with an international reputation as a financial centre, rooted in an Islamic environment.

However, not all Islamic finance countries have the strength to become superior in Islamic finance. According to the study conducted by the *Sharīʼah* fortune.com,[424] the most advanced countries in Islamic finance are listed as follows:

- Kuala Lumpur (Asia)
- Bahrain and Dubai (Middle East)
- London (Europe)
- Sudan (Africa)

The Islamic finance sector in Malaysia has been seen as the most progressive and attractive for investment with the offering of various incentives planned with further liberation in the coming years. Furthermore, the achievement of Malaysia's successful Islamic finance involves the entire sectors such as market institutions and Islamic financial products, capital flows, and strategic planning that establish the country's dominant position in the world of Islamic finance. Malaysia has also become the leading player in the global *Sukuk* (Islamic bond) market and in developing innovative products in money markets, derivatives, and in liquidity management.

The strong and comprehensive regulatory and supervisory framework is among the strong factors of the Malaysia's Islamic finance system. The factors include the stronger standard of corporate governance, disclosure, accountability, transparency, market discipline, risk management and customer protection. The key stimulating

[424] *Sharīʼah* Fortune, "Islamic Gold Preserve Your Money," retrieved on 18 August 2011, http://*Sharīʼah*-fortune.com/component/content/article/6-standard/26-islamic-gold-investment-preserve-your-money.

elements that drive the development of Islamic finance in Malaysia could be highlighted as follows:[425]

1. Stability: Malaysia has enjoyed political, social and economic stability consistently over the last 50 years that provide enabling environment to grow.

2. Government Support: continuous support by the government of Malaysia with dedicated laws, tax neutrality and tax incentives.

3. Central Bank: Central Bank of Malaysia has consistently driven Islamic finance development with comprehensive regulatory framework, institutional and infrastructure building and strong consumer education.

4. Approach of implementation: Gradual and incremental approach, for instance, the commencement of one Islamic bank, the permission for Islamic window license, and the liberalization of Islamic banks and the Islamic subsidiaries.

5. Stakeholders: Strong buy-in by relevant stakeholders (e.g., other regulators, financial players, the *"rakyat"* Muslims and non-Muslims alike).

6. Branding: Branding of Islamic finance as a business consideration as opposed to religious consideration and selling value proposition.

7. Innovation: Strong advocator of innovation and brave ideas – both domestic & international – *Sukuk* issuance, *Ar-Rahnu*, IFSB, IILM.

Although Malaysia has done sufficient measures comprising several initiatives in enhancing Islamic finance in Malaysia, a critical study is imperative to examine some issues regarding the incomplete matter such as the issue of harmonization in *Sharī'ah* deliberation and fatwas, the effect of liberalization towards the local market, and the

[425] Ahmad Hizzad Baharuddin,"The Regulatory Framework of Islamic Financial System in Malaysia," 10.

Sharī'ah product issues such as the BBA, which is still raising an issue among customers. Finally, it is worth to note that the study on Central Bank of Malaysia's initiatives in positioning Malaysia as a global hub for Islamic finance meets a finding as follows:

1. This study updates the recent policy taken by Central Bank of Malaysia regarding the development of Islamic finance in Malaysia.

2. This study found the existence of competition among countries in the world to become a leading country in Islamic banking and finance, which competition in fact benefits the system.

3. This study discloses lucrative information regarding the measures taken by Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic finance.

4. Finally, this study provides updated figures of Islamic banking and finance performance.

CHAPTER 5

ANALYSIS ON ISSUES AND CHALLENGES IN POSITIONING MALAYSIA AS A GLOBAL HUB FOR ISLAMIC FINANCE

5.0 INTRODUCTION

This chapter attempts to discover issues in Islamic banking and finance with focus on the issues raised as a result of the Islamic finance global hub policy. Hence, this study is expected to answer the third research question as stated in problem statement in chapter one. Further, as the study analyzed the Central Bank of Malaysia's effort in positioning Malaysia as an Islamic finance global hub country, hence, the analysis will begin with this topic. Subsequently, issues pertaining to Islamic finance global hub will be highlighted based on the literature reviews to provide the platform and background of the issues. Further, all issues were verified through interview series, which were conducted among the authoritative individuals such as the regulator, the Islamic finance scholars and the academicians.

5.1 Method of Analysis: Interview

This study applies interview method to verify related issues pertaining to this topic. Hence, several series of interviews were conducted with a number of prominent scholars and regulators. The following table details the description of all respondents:

Table 5.1: Details of Interviewees

Tag	Respondents	Institutions	Designation	Date of Interview
R1	Dr. Zainul Hasfi	Central Bank of Malaysia	Deputy Director of Islamic Banking and *Takāful* Department of the Central Bank of Malaysia	31 May 2013
R2	Mr. Makhzani Mustapha Ng.	Central Bank of Malaysia	Manager, Prudential and *Takāful* Section of Islamic Banking and *Takāful* Department Central Bank of Malaysia	14 March 2012
R3	Dr. Ronald	Islamic Financial and	Researcher in IFSB	25 April 2013

	Rulindo	Services Board	Secretariat	
R4	Dato' Dr. Mohd Daud Bakar	Amanie Advisors	Founder and Chairman	2 September 2014
R5	Dr. Amat Taap Manshor	Finance Accreditation Agency (FAA).	Chief Executive Officer	3 September 2014
R6	Assoc. Prof. Dr. Lahsasna Ahcene	International Centre for Education in Islamic Finance (INCEIF)	Deputy Director, Centre of Research and Publication.	22 January 2015
R7	Prof. Dr. Mohamad Akram Laldin	International *Sharī'ah* Research Academy for Islamic Finance	Executive Director	28 January 2015

5.1.1 Interview Method

The interview provides a comprehensive and accurate data from different individuals consisting of respondents who have a direct involvement in the CBM's policy, together with a respondent from the Islamic Financial Services Board and the Islamic finance prominent scholars. All issues were verified of their formality through verbal questions proposed toward the respondents. The possible number of respondent was determined based on Cresswell[426], which views that the acceptable number of the interviewee is between 1 and 2 persons up to 30 or 40 persons.

5.1.2 Interview Validity and Reliability

Interview protocol was developed by the researcher to get the respondent's reaction towards the policy of the Central Bank of Malaysia in determining the direction of the Islamic financial sector in Malaysia, especially in positioning Malaysia as an Islamic finance global hub. This method was applied in order to get evidence and confirmation on the policy of Central Bank of Malaysia and the related issues accordingly.

The interview process began with the appointment of the interview dates between the researcher and the respondents. Then, the permission was acquired from all

[426] Cresswell J.W., *Educational Research – planning, Conducting and Evaluating Quantitative and Qualitative research*, Ed.2, (New Jersey: Pearson Merril Prentice Hall, 2005), 375.

respondents to record the discussions using a voice recorder and written notes. Further, the interview data were compiled and subsequently analyzed accordingly. This analysis began with the transcription of the interview data in verbatim the way the questions were answered verbally by the respondents. The raw data were transcribed on paper and subsequently coded.

Then, the data were categorized after having a reduction process, based on specific themes. This data analysis is consistent with content analysis proposed by Patton.[427] The data are displayed using the Conceptual Clustered Matrix, as proposed by Miles and Huberman.[428] The outcome themes were analyzed based on case-by-case and cross-case analysis.

5.2 Analysis on the Central Bank of Malaysia's Initiative and the Government Supportive Factors in Promoting Malaysia as an Islamic Finance Global Hub

As stated in the Financial Sector Master Plan phase III, Central Bank of Malaysia has liberalized the Islamic financial market. This phase is considered as the beginning of a new foreign competition. This is the result to the intensifying degree of global competition and greater assimilation into the global arena. Thus, domestic banking sector needs to be prepared for greater liberalization.[429] This phase started when Malaysia opened up its banking industry to new international players in line with the World Trade Organization (WTO) liberalization program.

The liberalization of Malaysia's Islamic banking market commenced with the opening of the first foreign Islamic bank in August 2005. Subsequently, all Islamic banking windows converted into the full-fledged Islamic banks in 2007 as reflected in

[427] Patton, M.Q., *Qualitative Evaluation and Research Method*, (California: Sage Publications, 1990).
[428] Miles, M.B. & Huberman, A.M. *Qualitative Data Analysis*, Ed. 2, (Thousands Oaks: Sage Publications, 1994).
[429] *Ibid.*

the increasing domestic focus on Islamic banking business, supported by clearer accountabilities under separate Board and management structures.[430]

For the time being, Malaysia has 17 full-fledged Islamic banks. Three of the full-fledged Islamic banks are foreign-owned banks such as the Kuwait Finance House (Malaysia) Bhd., Al-Rajhi Banking & Investment Corporation (Malaysia) Bank Bhd. and Asian Finance Bank Bhd.

Central Bank of Malaysia has initiated the Malaysia International Islamic Financial Centre (MIFC) in August 2006 with the objective to promote Malaysia as a major hub for international Islamic finance. Among the measures taken by Central Bank of Malaysia with the support of the Malaysian government to promote the country as an Islamic finance global hub are:

1. The Establishment of the Malaysia International Islamic Financial Centre (MIFC).
2. Strengthening *Sharī'ah* factors.
3. Developing the Centre for Human Capital Development In Islamic Finance.
4. Supportive factors (Government support through tax incentive, environment support, cost of operation and accessibility).

The liberalization of Islamic financial center is clearly aimed at positioning Malaysia as a financial center hub for Islamic finance. This is based on Malaysia's expertise in a holistic system of Islamic finance consists of Islamic banking system, *Takāful* and Islamic financial market such Islamic capital market and Islamic money market.

This topic has raised concern on the measures taken by the Central Bank of Malaysia, whether the measures were sufficiently or requires more efforts to succeed

430 Pricewaterhouse Coopers, "*Malaysia, Asia's Islamic finance Hub*," (Kuala Lumpur, Malaysia: PricewaterhouseCoopers, 2008), 37.

the Islamic finance global hub plan. The following study shows the respondent's view pertaining to this topic.

5.2.1 Analysis and Results

In an interview with the Central Bank of Malaysia personnel R1, he insisted that the prime objective of financial liberalization in Malaysia is to position Malaysia as an Islamic finance global hub in specific and not aiming at becoming as a conventional financial center. Through this objective, Central Bank of Malaysia issued licenses to a number of foreign Islamic banks and financial institutions to operate in Malaysia. Malaysian clients, nowadays, have multi-choices in determining the desired financial institutions they opt to. This strategy promotes Malaysia as a country offering Islamic banking and finance system. R1 stressed that:

> *".....meaning that, we are not international center for conventional, but International for Islamic financial centre. It means that Malaysia has allowed international Islamic banks to open whether the branches or subsidiary. The International Islamic banks such al-Rajhi and Kuwait Finance House (KFH) can open as many as branches they wanted in Malaysia with the approval from the central bank of Malaysia"*

It is obvious to highlight that Malaysian government and the central bank are keen in developing Malaysia as an Islamic finance Global Hub, which is not only focusing on financial services, but also in other related areas such as Islamic finance education, Islamic finance regulation and others.

R1 Added:

> *"Another thing we want to be a center for reference. Reference center which could be top leader in Sharīʼah matters, the Arbitration Centre, resources center and product innovative place. Meaning that we want our Islamic financial industry to lead others, means that for instance ISRA as research institutions must has link to other Islamic research institutions in doing research. We also want to export our talent and make*

> *them job opportunity available for anytime. It could give our talent some sense of appreciation."*

The above statement clearly mentions the pathway of the Central Bank of Malaysia in developing Malaysia as an Islamic finance global hub country. Hence, the enhancement of all related sectors is vital to portray Malaysia as a place where a comprehensive Islamic finance system exists.

In another interview session with R2 on the intensive effort taken by the Central Bank of Malaysia in opening domestic market to foreign financial institutions, the financial liberalization in Malaysia, does not only involve the banking system per se, but also includes the *Takāful* sector. Through the Financial Sector Blueprint 2000-2010, Malaysia has allowed foreign *Takāful* operators to open their business inside the country.

R2 stressed that:

> *"Over the years, Malaysia has successfully established a firm foundation for the Takāful industry to grow and will continue to enhance the landscape in order to facilitate the growth of the Takāful industry, in line with the aspirations of the MIFC. The intended 'pathways' for the Takāful industry is embedded within the recently issued Bank Negara Malaysia Financial Sector Blueprint 2011-2020. For the Takāful companies, they should not be content with whatever developments or achievements thus far and must continue to maintain, improve and innovates their products and services."*

Currently, there are two foreign *Takāful* operators operating in Malaysia, namely; AIA Public *Takāful* Berhad and Great Eastern *Takāful* Berhad. One of the benefits of the emergence of foreign *Takāful* operators is that competition between local and foreign *Takāful* operators will provide Malaysian's clients various choices to opt the best service of *Takāful* operators. In terms of products, it might be a similar product offered by local and foreign *Takāful* operators, but the advance of technology and the fast quality of services may differ from one to another operator. Hence, the presence of foreign *Takāful* operators will steer to a positive competition in providing services to the customers. Among the products available in the market are savings, employee benefits, protection and a product mix such as protection plus investment.

To emerge as a financial center, the authorities are required to intensify promotion to position the country as a financial center. There are a lot of perfect factors that Malaysia has which contributing Malaysia's development. The effectiveness of infrastructure, the advanced of technology, the availability of nature sources and many other advantages compare to other countries. In a comment by R7, he agreed that the Central Bank of Malaysia and the government of Malaysia as well have undergone adequate measures to position Malaysia as an Islamic Finance global hub. R7 said:

> *"......i think in term of regulator, in term of government support, it is good, but the dynamicity of the industry itself......meaning the barriers... ."*

This view is consistent with R6's view in terms of the adequacy of measures that has been undertaken by the Central Bank of Malaysia for its global hub vision. This is evidence through a huge amount of fund that has been spent in many areas of Islamic finance such as the establishment of a world class education and training centers for Islamic finance with the establishment of the INCEIF and ISRA, the promotion through MIFC, the attractive tax charges, the liberalization of the Islamic finance system and many more. R6 insisted:

> *"I think a… what have been done so far…it is very impressive to frankly speaking, and one of them is the INCEIF and one of them is ISRA, and this is a high cost, if you look at the cost you know, because we are talking about the hub, we are not talking about the institution, or the bank …we are talking about the hub....we are talking about the market, so meaning that, a….a…bank Negara is putting a lot of money, and putting a lot of cost to maintain the status of being the hub…."*

R6 added that the establishment of many centers of the Islamic finance such as the higher education and training center is among the evidence of the measures taken by the Central Bank of Malaysia. R6 stressed that:

".....you have inceif, you have isra, you have ibfim, you have mif (Malaysia institute of finance) , mmm….you have this fstep and you just name it you have picked it, so many, you have mifc and you just name it, so many institutions, many initiatives you know, mmm…that doing in a different dimensions.... educations, aaa….training, aaa accreditation….standards…so the comprehensiveness…that aaa…the central bank is going through…..to ensure that you have number one, adequate, scope and sufficient and all the gaps has been basically aaaa breached….you know you have represent yourself as a hub... not only in banking, in education and in the standard and so on so forth. This is what you have seen the initiative recently frankly speaking it was impressive and a lot of money was injected you know… to issue this kind of facilities and that reflect Malaysia as the first place as a hub."

However, for further initiatives, there are some ideas and recommendations for the Central Bank of Malaysia to look forward in sharpening the strategy to realize the Islamic finance global hub vision. R6 suggested that the Central Bank of Malaysia should consider the expansion of their sub-entity service abroad such as opening the INCEIF outside Malaysia to provide education and training in Islamic finance.

R6 Suggested that:

".....there are more things to do ....i think….enhancing this one and the expending them .....and the ...maybe aaa.....how to say give them more support to go more internationally. For example maybe to have the branches....."

R7 perceived that it is important to look forward on the expansion of local Islamic finance institutions abroad. R7 says:

".......we should not be in our cocoon….we have a lot of qualities…we have a lot of good things we are doing we should expand outside….".

R7, also insisted that there is a lack of promotion initiatives taken by Malaysian authorities in promoting Malaysia as a global hub for Islamic finance. This is based on a comparison with Malaysian's southern neighbor, Singapore in promoting the country to the global investors. R7 observed that the initiatives taken by Singapore are more aggressive rather than what has been done by Malaysian authorities. R7 said:

" I think Singapore....., they are more aggressive…More aggressive in in term of...marketing…in term of reaching to people…in term of telling people what they are doing ….you see and they are known ...in financial market...they are known…Singapore, Hong Kong, ..they are

known… as a financial hub….so in term of Islamic finance we supposed to be like that … but we are not aggressive enough …….”

As a conclusion from the above study, it is obvious to notice that the Central Bank of Malaysia is keen in developing Malaysia as an Islamic finance global hub country. This is based on the views by R1 in insisting a clear direction by the CBM to move forward in realizing this vision. In addition, R2 insisted that CBM has taken measures to liberalize the *Takāful* market sector to be included in the Islamic finance global hub agenda as stated in phase III of Financial Sector Masterplan 2000-2010. Taking into consideration to the views by Islamic finance scholars, R6 and R7 agreed on the adequacy of measures taken by the CBM to position the country as an Islamic finance global hub. However, for the further measures, R6 and R7 suggest that CBM should undertake further initiatives to expand certain services to the global market like urging local Islamic financial institutions to open branches abroad and taking initiatives to establish its Islamic finance education and training center outside of Malaysia. Furthermore, R7 added that more aggressive promotion is required to promote Malaysia as an Islamic finance global hub country.

5.3 The Analysis on the Requirements for the Establishment of Islamic Finance Court

Since the inception of the Islamic banking in Malaysia in 1983, all legal disputes in Islamic banks are handled under the civil court purview. This is due to the jurisdiction of Malaysia that classifies the finance and banking matters under the financing matters and not Islamic matters. Islamic law in Malaysia is under the state purview and is only applicable to family law and “religious offences.”[431]

[431] Look at Schedule 9, list 2, Federal Constitution 1957.

The *Sharī'ah* court is only applicable to Moslems as stated in the *Sharī'ah* enactment, which indicates that the *Sharī'ah* Courts "shall have jurisdiction only over person professing the religion of Islam." However, this meaning is not applicable to Islamic banking, and hence, even both parties involve in a legal dispute are Muslims, the cases are maintained under the civil purview. For instance, in legal dispute between *Mohamed Habibullah bin Mahmood v Faridah Dato' Talib*, the judgement of the Supreme Court ruled that the *Sharī'ah* Court can only give a decision on the matters falling under its jurisdiction. As such, the amendment to Article 121 of the Constitution does not take away the jurisdiction of the High Court in matters when they fall under the Federal list. Such matters include banking and finance.[432]

Hence, any cases related to the Islamic finance shall be submitted under the jurisdiction of the civil court (either under the Malaysian statutes law or the English law). As usual, the *Sharī'ah* court handles on family matters. Problems may exist if the financing cases are being set under the *Sharī'ah* court jurisdiction such as the lengthy requirements of the evidential processes in financing matters and other things.[433]

However, the argument is also subjected to the Islamic finance under the civil court. It happens due to the lack of Islamic finance knowledge among the judges, the solicitors and the advocates. Indeed, the present act of IBA 1983, however, is not exhaustive and needs more clarification and interpretation by the Civil Court.[434]

Several court decisions in the past show this issue. As on 18 July 2008, the judge, the Honorable Datuk Abdul Wahab Patail decided that the home financing based on *al-Bai' Bithaman Ājil* instrument is not a *bona fide* sale but a financing transaction, which rendered the profit derived under the financing scheme. This is contradictory to

---

[432] Norhashimah Mohd Yasin, "Islamic Banking in Malaysia: Legal Hiccups and Suggested Remedies," *IIUM Journal*, (Vol.9, No.1, 2001), 6.
[433] Fakihah Azahari, "Islamic Banking: Perspectives on Recent Case Development," *Malayan Law Journal*, (16 February 2009), cxiii.
[434] Norhashimah Mohd Yasin, "Islamic Banking in Malaysia: Legal Hiccups and Suggested Remedies," 8.

the Islamic Banking Act 1983 (the IBA 1983) or the Banking and Financial Institutions Act 1989 (the BAFIA) as the case may be.

Basically, the BBA financing scheme is approved under the *Sharī'ah* principles, hence, it becomes critical for the court to understand the exact meaning of the term "Islam" and "Religion of Islam" in the way to determine whether the BBA complies with Islam or *vise versa.*[435]

However, the court's decision contradicts to the previous deliberation issued by the *Sharī'ah* Advisory Council of the Central Bank of Malaysia on the permissibility of *Bai' I'nah* in the BBA contract. As *Bai' I'nah* is a permissible contract, hence, the implementation of the contract has been used in the Islamic banking and Islamic capital market system. Even though some scholars disallow the implementation of the *Bai' I'nah* due to its tendency to *Riba*, some Islamic scholars permit the implementation of the contract as long as *Bai' I'nah's* pillars and conditions are being fulfilled. Based on the scholar's view on the permissibility of *Bai' I'nah*, hence, this contract has been implemented in Malaysia in order to provide more variety in Islamic banking products to become competitive to its conventional system counterpart. In the current practice, *Bai' I'nah* concept is widely used in Islamic finance transactions such as in bond issuance, credit card facility, money market transaction and debt securitization.[436]

The *Bai' I'nah* concept was first approved by the SAC on 12th December 1988 based on the proposal to use *Bai' I'nah* in the Islamic Inter-Bank Money Market.[437] Although all Islamic finance products are approved by the SAC, the civil court is still reluctant to follow the SAC deliberation. Due to this issue, the Central Bank of Malaysia has made an amendment on the Central Bank of Malaysia Act 2009 (Act 701) which later on gives the authority to the SAC to be referred to as the Highest and sole

---

[435] Fakihah Azahari, "Islamic Banking: Perspectives on Recent Case Development," xciv.
[436] *Ibid.*
[437] Bank Negara Malaysia, *Sharī'ah Resolution of Bank Negara Malaysia*, 1st Edition, (Kuala Lumpur, Malaysia: Bank Negara Malaysia, 2007), 15.

authority in dealing with Islamic Banking and Finance cases and all decisions made by the SAC are binding to the court.

This new legislation was gazetted on September 3, 2009 after receiving the royal assent.[438] One idea could be pondered upon to enhance the Islamic finance legislation is through the establishment of an Islamic finance court. However, the function of this court is not similar to the current *Sharī'ah* court under the state purview, which covers the matter around marriage, divorce and other matters alike. This court is assumed to provide enough personnel backed with Islamic finance knowledge.

The setting up the Islamic finance division under the High Court is called for to properly manage the Islamic finance cases. The establishment of the Islamic Finance court will provide sufficient talent in dealing Islamic finance cases. The judges, the advocates and the lawyers of the Islamic finance division must be those who have ample understanding in Islamic Finance knowledge besides their legal background. Nevertheless, the establishment of Islamic High Court does not mean attempting to interfere with the *Sharī'ah* court's jurisdiction under the state authority, which is limited to Moslem's family cases, but to provide the best solution for Islamic finance cases.

5.3.1 Analysis and Result

Several series of interviews were conducted with several authorities to seek their views pertaining to the issue of Islamic finance court. The respondents provided different views regarding the necessity of the establishment of the Islamic finance court. Some respondents stated that the number of Islamic finance cases is rather small and as such is not yet sufficient to lead to the establishment of an Islamic finance court. R1 and R3 shared the same opinion where the number of cases is among the vital factors to be taken into consideration prior to the establishment of an Islamic finance court. R1 said:

[438] Zulkifli Hasan, "Sharia Governance in Islamic financial institutions and the Effect of the Central Bank of Malaysia Act 2009," *Journal of International Banking Law and Regulation*, (J.I.B.L.R 105, Issue 3, 2010), 2.

> *"It needs in depth study to establish Islamic finance court, the reason is on the number of cases, where in the situation of lack of Islamic finance cases, there is no point to have Islamic finance court."*

The above opinion is similar to R3. With this regard, R3 responded:

> *"Question wether the Islamic finance court is in need or else, must reflect to the number of cases in the country. If the cases are not achieving the level to function an Islamic finance court, hence the current civil court is adequate to handle the Islamic finance cases.....countries like Sudan and Iran having Islamic finance court due to their policy of fully application of Islamic finance system. Whilst, in countries where the Islamic finance service represent 20 percent from total market shares, it is inefficient to establish an Islamic finance court. However, if the shares of Islamic finance increase up to 50 percent, then the Islamic finance court is needed."*

From the above statement, it is can be concluded that current legal issues in Islamic finance are still not yet up to the level that requires the establishment of an Islamic finance court. Based on R3 view, the number of cases influenced the decision to establish Islamic finance court.

R7 also gave a reason why an Islamic finance court is currently not needed because the fast clearence of Islamic finance dispute issues in the court. Based on his observation, there is no backlog cases in Islamic finance. R7 said:

> *".. our court has no backlog ..."* and added "*...you see…most of the cases, settled rapidly …and one of the reason why, people don't go to arbitration in Malaysia, because …Islamic finance cases….settled fastly in court….it doesn't drag…there is no back log… there is no back log for a many years or no delays or else...."*

The reason why there is no backlog in current Islamic finance cases is probably because most of the cases are not the complicated cases. Most of the cases were on the claims by Islamic bank against their defaulters. Hence, R7 viewed that for the time being, there is no requirement for the establishment of an Islamic finance court. R7 said:

> *"At this junction we don't really need because we already has a dedicated high court on Islamic finance..….I think that is good enough….that is good enough…I mean….. to certain extent it is similar*

to have a dedicated court for Islamic finance because after all most of the cases of Islamic finance cases….it is recovery cases where.....it is more to a debt's claim, Banks approach the court to claim their debts....that's all ...in most cases….mostly…..maybe 80 percent like that…all are recovery ….and then the defaulters…then…such cases are the simple cases…that's why I can anticipate there is no backlog in sum....because of ….it is a simple case…so….the court already knows…..mmm…they just need to certain …the claim of the bank is genuine claim….yes…and then….apart from that…so in term of court….it is not a big deal.

However, in term of documentation wise, it is inconsistent to document the Islamic finance contract under the purview of the conventional law. To some extent, it is peculiar in terms of the documentation issue. R7 said that:

"...any Islamic finance contract ….. this document is subject to Malaysian law…..Malaysia Islamic finance law or whatever…mm…like current English law….english law…English law…mostly…the document is Islamic finance…but…(under) the English law.….that is from one angle ….."

Hence, R7 insistsed:

".........we must ensure that people have confidence in our judiciary system….that may reflect to a political side…it is not being seen….you see…there is some political interference in the judiciary or ....what else…because that matter is very much in tact……because when people look at judiciary system…. They don't look at the Islamic finance cases ...you see…they will look at the entire judicial systems….thus the judicial system really independent or not…..sometime we might be independent we might claim to be independent but we must also be seen as the dependent…that is important…..that why…this is …this is…because ….so..so…that when people ...because it is not easy for you to get people…why..we say nowadays they put English law as the law to govern the document…because they know, they go to English court……I mean they have no worries about political interference …or any interference like….. executive interference we say…because they have the confidence in the systems. We need to go up to that level."

The above three respondents agreed on the unnecessity of the establishment of the Islamic finance court. However, R6 viewed the importance to have a robust Islamic finance regulation, which is considered as the robust facilities and a comprehensive system of Islamic finance. R6 insisted the public awareness on the litigation. R6 stressed:

"……..because that is important, people ...you know…they are always worried about in case of litigation in case of conflict and in case of disputes, what they do? So if you don't have adequate and transparent and strong legal framework or superior court..."

It could be concluded that the establishment of an Islamic finance court is vital but must be based on the number of cases and the complexity of the cases, which require the establishment of an Islamic finance court. A strong regulation of Islamic finance is important to ensure the sustainability of the system. Islamic finance court could be the completion of the Islamic finance regulation, which will enhance the Islamic finance jurisdiction. However, the establishment of an Islamic finance court in the practical situation must consider the availability of the cases.

5.4 Competition Between Local and Foreign Islamic Financial Institutions

In the early period after the independence of Malaysia, in 1959, there were 18 foreign banks operating in the country from the total of 26 commercial banks. The British and Chinese overseas banks owned these banks. There were 99 bank branches at that time and their core business was financing the local and international companies. The banks also provided working capital to large firms.[439]

The huge number of foreign banks controlling Malaysia's banking system had raised concern and urgency to the government. The government started to implement measures to control foreign banks by the introduction of two policies, namely licensing and requirement for prior permission to open new branches, which eventually reflected in the reduction of foreign banks in Malaysia. As at the end of 1973, the number of domestic banks was seventeen while there were nineteen foreign banks. The registration of domestic banks increased in comparison to the year 1958 in which there were only

[439] Saiful Azhar Rosly, *Critical issues on Islamic Banking and Financial Markets: Islamic Economics, Banking and Finance, Investments, Takaful and Financial Planning,* (Kuala Lumpur, Malaysia: Dinamas Publishing, 2005), 221.

eight domestic banks.[440] During the 1973 period, there were no licenses given to new foreign banks. In 1983, there were 16 foreign banks indicating the reduction of 3 banks from the year 1973.

The current trend of globalization and financial liberalization needs foreign participation in banking activities in Malaysia. To move ahead with this trend, the Central Bank of Malaysia made an announcement on the open policy towards foreign banks. The question on how foreign banks would dominate the banking business depends on the ability of domestic banks to compete in the marketplace.[441]

The relative absence of controls on the base lending rate (BLR) and interest on deposits would show how domestic banks survive in the midst of the aggressive moves of foreign banks to capture new markets. Bear in mind that foreign banks are simply exportable, meaning that they are not given protection by any quarters, and therefore expected to be efficient and highly competitive. They have operated elsewhere around the globe and understood well what to do in the event of crisis. [442]

As in 2009, the CBM had issued 16 Islamic banking licenses, 10 licenses to local banks and 6 to foreign banks. The local Islamic banks are; Affin Islamic Bank Berhad, Alliance Islamic Bank Berhad, AmIslamic Bank Berhad, Bank Islam Malaysia Berhad, Bank Muamalat Malaysia Berhad, CIMB Islamic Bank Berhad, Hong Leong Islamic Bank Berhad, Maybank Islamic Berhad, Public Islamic Bank Berhad and RHB Islamic Bank Berhad. Another six licenses were issued for foreign banks, namely; Al-Rajhi Banking and Investment Corporation (Malaysia) Berhad, Kuwait Finance House (Malaysia) Berhad, Asian Finance Bank Berhad, HSBC Amanah Malaysia Berhad, OCBC al-Amin Bank Berhad and Standard Chartered Saadiq Berhad.

The aim of the CBM in issuing Islamic Banking licenses separately was driven by *Sharī'ah* requirement for greater compliance. Doing different systems in one place

[440] *Ibid.*
[441] *Ibid.*
[442] *Ibid.*

caused the ambiguities (*gharar)* especially in the area of profit generated from the business.[443]

CBM also issued five licenses for International Islamic Banks to cater global needs. The banks are Unicorn International Islamic Bank Malaysia Berhad, PT. Bank Muamalat Indonesia Berhad, Tbk., Al-Rajhi Bank KSA, Deutsche Bank AG and Elaf Bank B.S.C (c). This study analyzed the competition of local and foreign Islamic finance institutions. However, it may not include the International Islamic Banks as their business segment as it is different from the local business as well as their different client base. Furthermore, the foreign banks entry is just like a coin with two sides. It either brings harms or potential benefits to domestic banks.

Some researchers viewed that the participation of foreign bank in domestic market may enhance the functioning of national banking markets in the long run and benefit local banking customers. However, in some cases, foreign entry can also result in the risk exposure. This will happen through the competition among banking institutions, which leads to the lowering of profits by domestic banks and reduce their charter values and put them into a vulnerable situation. Foreign bank entry may also cause an uncertainty and as such destabilize the financial system mainly in the poor regulations and supervisions. In order to benefit from the participation of foreign banks, some measures could be taken such as the formation of strong regulations and supervisions with more preparation by the policymaker to enter the liberalization program.[444]

However, other researchers' studies on Malaysia's experience regarding the banking competition with foreign banks found that the level of efficiency is held by

[443] Mohamad Abdul Hamid, Noor Inayah Yaakub, Wan Kamal Mujani, Mohamed Sharizam and Kamaruzaman Jusoff, "Factors Adopting Islamic Home Financing: A Case Study Among Consumers of Islamic Banks in Malaysia," *Middle-East Journal of Scientific Research* 7 (Special Issue of Diversity of Knowledge on Middle East, IDOSI Publications, 2011), 48.

[444] Stijin Claessens, Asli Demirgguc-Kunt and Harry Huizinga, "How Does Foreign Entry Affect Domestic Banking Markets?," *Journal of Banking and Finance*, (Vol.25, Issue 5, 2001), 891-911.

domestic banks rather than foreign banks. This achievement indicates sound and good management and efficiency of domestic banks in controlling their costs.[445]

In another study conducted by Sok-Gee Chan and Mohd Zaini Abd Karim,[446] the study found that Malaysia exhibits good performance of foreign banks' operation compared to other Southeast Asian region countries such as Indonesia, Philippines and Thailand. Although there are no significant differences in average cost efficiency among the countries, foreign banks in Malaysia made more profits and function more efficiently as compared to others. Perhaps, this advantage is due to the high economic freedom in Malaysia over the years. Malaysia also implements investor friendly policy with lower trade restriction, which might contribute to the efficiency of foreign banks. This policy allowed foreign banks to bring more capital into Malaysia. In contrast to other ASEAN countries, there have been governments' controls over the banking sector since 2004.

This study, however did not find previous studies conducted to determine the impact of foreign Islamic banking institutions towards domestic banks in Malaysia. Therefore, in order to analyze the competition among Islamic banking institutions in Malaysia, a set of bank's performance schedule based on Return on Asset (ROA) and Return on Equity was analyzed as follows:

Table 5.2: Average Performance of Islamic Banks (2001-2009)

BANKS	**ROA****	**L/F***	**BANKS**	**ROE*****	**L/F***
MAYBANK ISLAMIC	4.17	L	BANK ISLAM	77.62	L
ALLIANCE ISLAMIC	1.44	L	AFFIN ISLAMIC	13.56	L
AMISLAMIC	1.17	L	AMISLAMIC	12.19	L
RHB ISLAMIC	0.90	L	MAYBANK ISLAMIC	11.05	L
HSBC AMANAH MALAYSIA	0.83	F	RHB ISLAMIC	10.77	L
HONG LEONG ISLAMIC	0.81	L	ALLIANCE ISLAMIC	9.98	L
AFFIN ISLAMIC	0.63	L	HONG LEONG	9.48	L

[445] Ong Tze San, Lim Yee Theng and The Boon Hong, "A Comparison on Efficiency of Domestic and Foreign Banks in Malaysia: A DEA Approach," *Business Management Dynamics Journal*, (Vol.1, No.4, Oct 2011), 33-49.

[446] Sok-Gee Chan and Mohd Zaini Abd. Karim, "Efficiency of Foreign Banks: Evidence from Selected (Association of Southeast Asian Nations," *ASEAN Countries, African Journal of Business Management*, (Vol. 5 (14), 2011), 5617-5626.

			ISLAMIC		
PUBLIC ISLAMIC	0.53	L	PUBLIC ISLAMIC	9.21	L
STANDC SAADIQ	0.42	F	HSBC AMANAH	5.54	F
EONCAP ISLAMIC	0.38	L	EONCAP ISLAMIC	5.24	L
BANK MUAMALAT	0.24	L	BANK MUAMALAT	4.42	L
OCBC AL AMIN	0.15	F	CIMB ISLAMIC	3.76	L
BANK ISLAM	-0.06	L	OCBC AL-AMIN	3.66	F
CIMB ISLAMIC	-0.29	L	STANDC SAADIQ	2.79	F
ASIAN FINANCE	-0.57	F	ASIAN FINANCE	-1.62	F
AL-RAJHI	-7.66	F	AL-RAJHI	-17.73	F

Source: Bankscope Database
*L/F: Local/Foreign
** Return on Asset
*** Return on Equity

Table 2 shows the average size of Islamic banks in Malaysia from 2001 – 2009. In average, the performance of Islamic banks based on the ROA is dominated by five banks, headed by Maybank Islamic bank and followed by Alliance Islamic bank, AmIslamic bank, RHB Islamic bank and HSBC Amanah Malaysia bank.

However, the calculation based on Return on Equity (ROE) shows different result where Bank Islam Malaysia Berhad (BIMB) headed the list, followed by Affin Islamic bank, AmIslamic bank, Maybank Islamic and RHB Islamic bank. In conclusion, the above table shows that local Islamic banks in Malaysia performed better compared to other foreign Islamic banks. Overall, Maybank Islamic bank as a local bank enjoys lucrative position to become as the top local Islamic banks followed by others, namely Alliance Islamic bank, AmIslamic bank and RHB Islamic banks. A foreign Islamic bank, HSBC Amanah ranked fifth.

The competition between foreign and local Islamic Finance institutions promotes a good quality of services that provide customers a wide option to choose from. The regulator creates this kind of competition to ensure that the best services could be provided to the customers. Thus, the phrase that says, “competition makes thing perfect”, is indeed true. However, due to the financial liberalization effect towards local institutions, some measurement must be designed to secure local institutions from the impact of this competition. Some may argue, whether there is a mutual benefit that Malaysia can gain from the openness of its market or there should also be a mutual agreement to our companies to open subsidiaries in the market where the foreign financial institutions belong to.

In fact, the Central Bank of Malaysia's idea from this competition is to create innovative and progressive development of Islamic finance in the country. However, some protection plan is needed to secure the sustainability of domestic Islamic banking institutions such as the determination of a certain segment of the banking business for foreign Islamic banking institutions to get involve in. Thus, the future Islamic banking in Malaysia will continuously develop with a tough competition between local and foreign Islamic banking institutions.

5.4.1 Analysis and Result

From the interviews, R2, R3, R4 and R7 agreed that competition in Islamic finance industry is natural in the business. This competition happens in all sectors of Islamic finance such as Islamic Banks, *Takāful* and Islamic capital market. The liberalization of Islamic finance opens a direct competition between local and foreign financial institutions to increase the volume of customers. From the positive view, the presence of foreign financial institution will benefit local Islamic financial institutions in terms of technology and operational experience, which local Islamic financial institutions may learn from its foreign competitors. In an interview with R2, he said:

> *"I assume this means competition between TOs with foreign shareholding and (foreign) those without (local). The level of competition that exist is not only between foreign and local Takāful operators, but also amongst the foreign companies and amongst the local ones. The presence of foreign shareholders within the Takāful industry can bring about a positive effect. As these shareholders are mostly foreign insurers, they bring with them vast experience in management, product design, governance, marketing etc. The new paradigm brought about by the foreign Takāful companies can act as an example for the local Takāful companies to learn and even innovate themselves. In light of such positive competition, the benefits to reap will be enjoyed by all stakeholders."*

R3 responded that the number of Islamic banks in Malaysia must be based on the number of population and hence the competition among them will fair and will promote stability to the banking system. According to R3, the number of Islamic banks in Malaysia is adequate and perhaps exceeded the demand. R3 said:

> *"There must be competition if the domestic market is opened to foreign banks. Then, the consideration must also include the market share of the country. For instance, the population in Malaysia is about 27 million. Thus, the banks must also equal to the number of population. Then research needs to be done to evaluate how much the banks according to the number of the population. If you look at Malaysia, the existence of Islamic Banks has exceeded the appropriate number."*

R4 stressed that it is difficult to eliminate competition in any business environment, which is not only regarded as a financial institution per se, but other business entities are also competing with each other. The competition is compulsory and each party has to face it in whatever type of business it is. R4 insisted that the wrong message regarding the competition in Islamic finance is conveyed causing this issue to become bigger although the actual situation is not as portrayed. R4 said:

> *"Competition is must. There is nothing around the world without competition. For example I'm wearing shoes. The shoe's manufacturers also competes each other. So, there is no issue about the competition which it heard such a big thing due to wrong message delivered by the mass."*

R7 stressed that although the liberalization policy allows competition between foreign and local Islamic financial institutions, the protection measure towards local Islamic financial institutions must also be included in the liberalization plan.

> *"….we need to protect the local industry…we need to…but in the same time … you might allow a foreigners to come but you give certain limitation……for instance…we say…in term of size…in term of number of branches…as example……you see… in term of what kind of service you can provide, you see…."*

In conclusion, all respondents agreed on the existence of competition, which appears as a result of the liberalization policy. However, some of the respondents viewed the requirement to ascertain limitation in order to secure local Islamic finance institutions such as the different segment of customers where foreign Islamic finance institution provide financing to the international business client's entities or the limitation of size. Competition, in one side, could enhance the quality of service, technology advancement, and precise operational management. However, the matter behind the competition is whether it is a fair competition or not. A fair competition, among others, means similar fund size, technology, and efficiency. This kind of competition is a fair competition where each party competes to provide the best services over others. An unfair competition is a competition between two or more Islamic financial institutions, which differ in the size of fund, the large gap of technology differences, the market segment and others. Hence, the regulator must ensure that the impact of liberalization policy will promote a fair and harmony competition between local and foreign Islamic finance institutions.

5.5 The Internationalization of Local Islamic Finance Institutions

With consideration of the Islamic financial liberalization in Malaysia, foreign Islamic banks are allowed to open their business in Malaysia and as a mutual co-operation, local Islamic banks should be allowed to open their business abroad. However, the questions arise on the capability of Malaysian Islamic banks to set up their branch oversees. There are several factors overwhelming local Islamic banks to go international with the consideration to the following strengthening factors, namely wide product innovation, risk control and regional sense.

A study conducted by Ismail Bin Abdul Rahman and Melati Ahmad Anuar[447] attempted to trigger the factor that motivates Malaysian Banks to go international. This study shows that most of the previous internationalization practices of Malaysian

[447] Ismail Bin Abd Rahman and Melati Ahmad Anuar, "What Motivates Malaysian Banks to Go International? A Case of Islamic Banking Products," (8^{th} International Conference on Islamic Economics and Finance, Doha Qatar, 19-21 December 2011), 1-15.

banking institution entering foreign countries as a wholly-owned representative office and subsequently transforming to branches or subsidiaries. In addition, the research found that in countries with unstable economic such as Vietnam and Cambodia, Malaysian's banking institutions are very detailed on their operational costs. In a country like China, Malaysian banks used to venture with local company as the country's regulation allows such co-operation. Nevertheless, this kind of venturing system also has a problem, especially in implementing the bank's corporate objective, caused by different ideas, strategies and cultures between one to another.[448]

In a study on the other factor such as product innovation, banks with more innovative products compared to other competitors, are likely to go abroad with the objective to establish more client-based using their advantages on product innovation and make it more economical.[449]

The geographical factor also became the main consideration for the financial institutions to go abroad. This study found that the location tradition is still being chosen among the multinational banks. For instance, Latin America, Italy or Portugal is a familiar location to Spanish multinational banks. Thus, the Malaysian financial institutions take this practice in their consideration to open branches and subsidiaries outside the country.[450]

In Malaysia, although, the size of Malaysian banking business is currently still small compared to other developed countries, the country has started to evolve in the regional area to become one of the active players. Thus, more preparation is needed to flourish the financial institutions with the capability to sustain in the regional economic recession and turmoil. Therefore, it is important to characterize an international bank as

---

[448] *Ibid.*, 15.
[449] *Ibid.*,1.
[450] *Ibid.*,12.

a bank with a high level of capital, extant cross-border activities and complexity of operations and commensurate with its size.[451]

Observing the opportunities of Muslim market is important to be addressed. Based on the record, 57 Moslems countries joined the OIC (Organization of Islamic Cooperation) representing 8.9% of the global GDP in 2012, which is US$ 6.4 trillion. These economies are also growing at a faster rate than the global economy. The projected growth of the OIC markets from 2013 through 2018 is expected to be an average of 6.3% compared to the global GDP growth averaging 5.3% (based on IMF projections) during that period.[452] Therefore, the purchasing power of Muslim countries cannot be undermined.

The top ten OIC countries by GDP are Indonesia, Turkey, Saudi Arabia, Iran, UAE., Malaysia, Nigeria, Egypt, Iraq, and Kazakhstan. A past assessment (2000-2010) on rapid-growth markets by an E&Y report shows that 10 of the top 25 real GDP growth markets had significant Muslim populations.[453]

The opportunity for Malaysian Islamic banks to expand oversea, especially in those countries are widely open. Since the Islamic funds in Malaysia represents more than 10 percent of the global Islamic funds, hence, the idea to go abroad is brilliant. However, full preparations and strategies must be in order. In terms of Malaysian Islamic banking products, some products are not suitable for middle-east application such as *Bai' I'nah* and *Bai' al-Dayn*, where both contracts are not acceptable to the Maliki, Hanbali, and Hanafi schools of thougt (madzhabs).[454]

These two contracts have given birth to many products such as those as listed below:

1. Personal financing and Overdrafts (*Bay' al-I'nah*)

---

[451] Bank Negara Malaysia, "BNM Guidelines, The Implementation of Basel III," retrieved on 28 August 2012, http://www.bnm.gov.my/guidelines/01_banking/01_capital_adequacy/12_nt_007_25.pdf.
[452] Zawya.com, "State of the Global Islamic Economy 2013 Report," retrieved on 23 February 2014, http://www.zawya.com/files/islamic-reports/tr-state-of-islamic-economy-2013.pdf.
[453] *Ibid.*
[454] Saiful Azhar Rosly, *Critical issues on Islamic Banking and Financial Markets: Islamic Economics, Banking and Finance, Investments, Takaful and Financial Planning,* 282.

2. Negotiable Islamic Certificates of Deposit (NICD) (*Bay' al-I'nah & Bay' al-*

Dayn).

3. Islamic Accepted Bills (*Bay' al-Dayn*).

4. Islamic Bonds (*Bay' al-I'nah & Bay' al-Dayn*)

Considering the above background, it is important for Malaysia to have many global accepted products. As some Malaysian Islamic banking products are not approved by other countries, especially in the middle-east, it is hard to give challenge to conventional banks in foreign countries due the deficit in the number of Islamic banking products. Normal Islamic banking products such as *Murābahah* and *al-Bai' Bithaman Ājil* already exist in other countries in the forms of home financing, trade and vehicle financing.[455]

In addition, a wide network for Islamic banks could be established through a strategic alliance between local and foreign Islamic banks. This networking tie could favor Islamic banks in terms of providing efficient services such as remittance services using an advanced money transfer technology that is linked with the global banking network. Among others, this connection will also improve efficiency, innovative technology and is good for marketing both partners-domestic and foreign Islamic banks.

Currently, none of the local Islamic banks has subsidiaries opened their abroad. However, the local conventional bank and the largest one in Malaysia, Maybank, has played an active initiative at the international level and opened its branches in over 16 countries, namely Bahrain, Brunei, Cambodia, China, Hong Kong, India, Indonesia, Myanmar, Pakistan, Papua New Guinea, Philippines, Singapore, Thailand, USA, United Kingdom and Vietnam.[456] In Indonesia, Maybank has opened Maybank Syariah Indonesia and it could be considered as the expanding of local Islamic banks

[455] *Ibid.*
[456] Maybank Website, retrieved on 7 February 2013, http://www.maybank.com/.

internationally. Perhaps, this could be considered as a pioneering effort in expanding local Islamic banks out of Malaysia due to Maybank's experiences in operating Islamic banking in its subsidiary in Malaysia, namely Maybank Islamic. While another Malaysia's domestic conventional bank like CIMB bank opened its branches in over 10 countries; Bahrain, Brunei, Cambodia, China and Hong Kong, Indonesia, Myanmar, Singapore, Thailand, United Kingdom and USA.[457] Other than Maybank and CIMB, there are no other Islamic bank in Malaysia that has opened their business overseas. Bank Islam, as the first Islamic Bank in Malaysia, is also focusing on the local banking business and there is no sign for the Bank to operate internationally.

5.5.1 Analysis and Result

As a respond to the question, R7 perceived that the internationalization of local Islamic finance institutions is important to show the strength of local IFI, which is not just competent inside the country, but also abroad. R7 said:

> "*As I said recently, you are not just a local player, we are not the home winner .....but we are present everywhere and people know our existence …people know that yes…*"

However, the internationalization of the local IFI depends on it business model. The business model of the IFI is among the main factors to expand abroad. Some IFI sees the urgency to expand abroad while others feel that it is adequate to maintain operation inside the country. It depends on the capability and the strategy of local IFIs. R7 stressed:

> *"Of course, some time goes back to bank's business model and so on …they will much depending on that model…"*

In response to the question whether there should be a mutual understanding between two countries to open their market, R6 expressed that the policy of mutual

[457] Banks Around the World, retrieved on 7 February 2013, http://www.relbanks.com/asia/malaysia/cimb-group/branches.

opening of the market is good, which perhaps helps to expand local IFIs abroad. Hence, it is not only one side decision to open and liberalize the market, but also an agreement from the counter country. R6 said:

> *"....and at the same time it is a good point you see, we can have a mutual agreement just like people come from Philippine and we go there, come from Thailand, we go there, same thing... encourage the local bank which already established that they can go abroad."*

At this point, it is clear to note that the liberalization policy of the local market should be balanced with the expansion of local IFIs abroad. The expansion will benefit the IFIs in term of new market exposure, more clients, strategic future plans to grab foreign market and as a catalyst to appear as a global player in the global market. Currently, the expansion of Malaysian IFIs could be seen in the regional of Southeast Asia. Perhaps, the condition of the regional market seems to become familiar to IFIs' shareholders. At this level, it is good as a starting point to go as far as possible to the other regions. The government and regulators could encourage local IFIs to expand abroad through a mutual agreement like the G2G agreement. This initiative will expand local IFIs business and create business opportunity in other countries.

5.6 Mega Islamic Bank

Among the prime strategic vision of the Malaysian Islamic banking industry is to establish a mega Islamic bank. This idea has been raised in 2006 and was seriously discussed among the top leaders in 2010 when the Governor of the Central Bank of Malaysia, Tan Sri Dr. Zeti Akhtar Aziz, mentioned this idea in the Global Islamic Finance Forum 2010, with the announcement of the issuance of a new license for a mega Islamic bank.[458] Prior to this, it was reported that Malaysia had determined two foreign banks to be licensed as mega Islamic banks with a minimum paid up capital

[458] The Star Online, "One Mega Islamic Bank This Year," retrieved on 2 September 2012, http://biz.thestar.com.my/news/story.asp?file= /2010/10/27/business/7303314&sec=business.

worth US$1 billion and become as a part of the Malaysian financial liberalization program as announced in 2009.

However, after such announcement up the CBM, this idea seems difficult to be realized due to several reasons. Two proposals have been recommended as a blueprint for the establishment of a mega Islamic bank. The first proposal is on the merger of local Islamic banks to subsequently become as a mega Islamic bank and the second proposal is on the foreign investment capital injection to set up the mega Islamic bank.

Subsequently, in March 2012, the Governor of the Central Bank of Malaysia, Tan Sri Dr. Zeti Akhtar Aziz announced the issuance of two licenses for Mega Islamic Banks. However, more time was given to the companies to study the strategic plans and risk mitigation strategy for the sustainability of the companies.[459]

The government of Malaysia is also concerned with the new development of this project as mentioned by the Minister of Finance II, Datuk Seri Ahmad Husni Hanadzlah in 25th of June 2012 to The Star news: "the setting up of mega Islamic banks in Malaysia will not merely serve the needs of the domestic economy, but also position the country as the benchmark in Islamic global finance."[460] It would also place Malaysia far ahead of other competing countries. The Malaysian Mega Islamic Bank also received sufficient support from the government as Husni said: "Under the National Key Economic Areas, financial services are among the economic growth sectors and it is also an area where we are competing with other countries."

An international Islamic economic scholar, Mr. Rushdi Siddiqui[461] responded on this topic and stressed that Malaysia needed to establish this mega Islamic bank to

---

[459] The Star Online, "Mega Islamic Bank Will Set Benchmark," retrieved on 18 September 2012. http://biz.thestar.com.my/news/story.asp?file=/2012/6/25/business/11543548&sec=business.
[460] The Star Online, "Mega Islamic Bank Will Set Benchmark," retrieved on 18 September 2012, http://biz.thestar.com.my/news/story.asp?file=/2012/6/25/business/11543548&sec=business.
[461] Business Times, "Where is Malaysia's Mega Islamic Bank?," retrieved on 20 September 2012, http://www.btimes.com.my/Current_News/ BTIMES/ articles/ Babyx /Article/index_html

remain as the industry leader. According to Rushdi, Mega Islamic bank will provide challenge to conventional banks like, HSBC, JPMorgan Chase, Standard Chartered, etc. to compete in mega projects, underwriting, advisory, etc., in OIC and G20 countries.

The idea of Mega Islamic bank has also triggered an interest in gulf countries. A talk on Mega Islamic banks was first made in 2009 with a proposal of $1 billion of paid-up capital for the initial set up. However, the project faced several delays. It is reported that the GCC countries also announced the establishment of Mega Islamic bank in 2012 with a paid up capital of $1 billion and expected to be headquartered in Bahrain. [462]

A debate on Mega Islamic bank continues. How would the bank function if it is really incorporated? How could the bank contribute to the Islamic finance industry considering the unfavorable participation of al-Rajhi bank? In fact, al-Rajhi is the world's largest Islamic bank as recorded in 2010, where the bank managed about $49.2 billion in asset.[463] A question also triggered the capability of Mega Islamic bank in competing with the global financial institutions that open Islamic banking windows or are involved in *Sharī'ah* compliance investments.

A proposal for the Mega Islamic bank's function was submitted by Dr. Rushdie Siddiqui to the the Islamic Development Bank President, Dr. Ahmad Mohamed Ali through a letter. The letter suggests an additional involvement of Mega Islamic bank in stock exchanges and trading platforms.[464]

#ixzz23n9HXK9L.

[462] Gulf Business, "New $1Bn Islamic Bank in Doha," retrieved on 22 September 2012, http://gulfbusiness.com/2012/04/new-1bn-islamic-bank-in-doha/#.UD74RpYs324.

[463] Emirates 247, "Mega Islamic Bank Maybe Launched 2013," retrieved on 25 September 2012, http://www.emirates247.com /business/ mega/-islamic-bank-may-be-launched-in-2012-2012-02-22-1.444362.

[464] Business Times, "Mega bank, stock exchanges and trading platforms," retrieved on 26 September 2012,

http://www.btimes.com.my/Current_News/BTIMES/articles/20120424011119/Article/#ixzz250ZiD5YE.

The rationale of this proposal is based on the following reasons:

(1) The capital charges associated with Basel III for now, as we are at the blueprint stage, and

(2) Mega Islamic bank implies cross border. However, without another mega bank, would there be counterparty (small) size risk issues, as the average of an Islamic bank's paid-up capital is equivalent to the assets under the management of an Islamic equity fund?

The Islamic finance system of "equitization" is needed to balance debts bias through *Sukuk*, *Murābaha* syndicate loans and others. Islamic finance too is not free from over-leverage as experienced by Bahrain-Based Islamic bank, ArCapita, which declared bankruptcy. There was also defaulted Sukuk, which became bankrupt. Thus, the risk management in Islamic finance is important and there is no such "divine put" in Islamic finance as well.

Dr Rushdie Siddiqui described the flow of economic system where the financing is vital for economies. However, for the purpose of future development in Muslim countries, the most important thing is on intellectual property-led engineering compared to financial engineering.[465]

Finally, the establishment of mega Islamic bank must take all considerations from various parties. Learning from the conventional mega bank is one of the ways to strengthen the Islamic Mega Bank. The collapse of the Lehman Brother as the global financier is something that the regulator has to ponder upon. Although the Islamic Bank applies a different system from its conventional counterpart, the huge amount of financing may bring the Mega Islamic bank into more risk. There is also hearsay among Malaysian bankers that a few of them rejected the Islamic Mega bank project. They view that the idea of an Islamic Mega bank in Malaysia is "embarrassing" as the local

---

[465] *Ibid.*

market is already very competitive.[466] The role of CBM in setting up the Malaysian Mega Islamic bank also raises several issues such as an increasing rivalry in the already competitive local market, while possibly deterring the entrance of foreign players, which is needed to boost internationalization of Islamic finance in Malaysia.[467] With an already competitive domestic Islamic banking market, dominated by a handful of major players, an Islamic megabank could further erode businesses instead of helping the market grow – always assuming there is in fact enough players to sustain such an effort at all.[468] Unless the function of Malaysian Islamic Megabank is different from local banks and purposely to finance global players, then the competition among local Islamic banks is something not to be worried about. There should be a certain restrain on the services provided by the Islamic Mega bank such as retail banking, which is mostly provided by current local Islamic banks. Therefore, the Malaysian Islamic Mega bank could become a reality after all the issues are resolved.

5.6.1 Analysis and Result

Several series of interviews were conducted to gather Islamic finance scholars', regulators' and practitioners' opinions regarding this issue. Most of the respondents are on view that the idea of the establishment of the Islamic Megabank is good but with certain limitations. According to R4, the establishment of the Islamic Megabank is a good idea to provide services for international clients but with a different business model from the local IFI to avoid an unfair competition. R4 responded:

> *"Islamic Mega Bank could be established to cater international segment of business clients but not to offer service in retail business and compete with local market. The business model of Megabank should be different to local Islamic banks."*

466 Redmoney, *Islamic finance News*, (Kuala Lumpur: Redmoney Publications, 2012), 12.
467 *Ibid.*
468 *Ibid.*

R7 specified the features of Islamic Megabank that must stand in a different field from other normal Islamic banks in term of the customers' segment. However, the Megabank should have a comprehensive products consist of retail, investment and other products to meet the feature of a Megabank. R7 explained:

> *"….Just like investment banking and all.....so...it must becoming like that one…so it is a different class…..you see…now we are talking about private banking… you see,, so it's target group must be different…just when you talk about mega bank …we expected it to have everything, it got retail….corporate banking also…just like HSBC, City Bank and all …. It got Islamic fund and everything and then it is qualified to name it as megabank…"*

R6 viewed the advantage of the establishment of Islamic Megabank, which can provide financing to global Moslem communities. R6 said:

> *"...Islamic Megabank is a good idea, provided we are talking about global……with global features like HSBC, City Banks, that is exist every-where and have operation in everywhere. That is good, to serve the muslim community and the …so on and so forth, but you have in Malaysia, you have to some extent sufficient ….you see…..mmm…*

R6 added that the presence of Islamic Megabank should exist in many countries and not just limited to one country.

> *But the focus of their operation should be internationally. Meaning that like HSBC ….so you look it everywhere .....so you can have a mega bank in Malaysia but in every-where... in US, in Bahrain in Saudi Arabia, in France, in Paris, in Berlin, in Europe, in Japan, in Hong Kong , in Singapore...."*

R6 stressed that the establishment of Islamic Megabank should not be limited to Malaysia but outside the country as well to cater a wider market of clients. R6 added:

> "*Not the mega bank within Malaysia and stay in Malaysia with close door, that one I think it is not a good idea."*

As a summary from the above discussion, it could be concluded that the Islamic Megabank is a very fresh idea proposed by Islamic finance scholars to establish a bigger size Islamic bank. Although the idea is originated in Malaysia, it does not mean to limit the establishment in Malaysia, but also to expand the business outside the

Malaysia. Opening the Islamic Megabank in Malaysia without expanding the business abroad will shrink the market size and harm ordinary banks. Hence, the business model of Islamic Megabank is to cater international clients through the establishment of branches outside Malaysia.

5.7 Human Capital Issues in Islamic Finance

The human capital shortage issue has been discussed frequently among Islamic finance employers. The shortage happened in various segments of Islamic banking and finance; *Sharī'ah* advisor, *Sharī'ah* officer, legal practice, regulation and supervision and in Islamic finance high education as well. Further, some of them claimed that there is not enough investment allocated to adequately prepare Islamic finance knowledge for the next generation.

There are many definitions and concepts, which describe human capital. According to the Organization for Economic Co-operation and Development (OECD)'s, human capital is defined as "*the knowledge, skills, competences and other attributes embodied in individuals that are relevant to economic activity*".[469] This definition encapsulates four key elements, namely knowledge, skills, competencies and attributes, which an individual should have to play a positive role in the economy. However it must be emphasised here that the term attributes should refer to the right attitude that is inculcated through ethics and moral values.[470] In 2009, the International Islamic University of Malaysia conducted a study on the demand for Islamic finance professionals and the result shows the need of Islamic talent will reach two million by 2020.[471]

---

469 Organization for Economic Co-Operation and Economic Development (OECD) , *Human Capital Investment: An International Comparison*, Paris, (OECD Publications, 1998), 9.

470 Agil Natt, Syed Othman al-Habshi, Mohd Pisal Zainal, "A Proposed Framework in the Human Capital Development in the Islamic Financial Services Industry," *The Journal of knowledge Economy & Knowledge Management 2009*, (Vol.1, Spring, 2009), 14.

471 The Star, "Talent Shortage in Islamic Banking," retrieved on 2 October 2012,

For a more specific figure on this, a report issued by Deloitte Islamic Finance Knowledge Centre in September 2010 highlights that only 4% of Islamic finance leaders agree that IFIs are properly staffed, 15% disagrees that IFIs are properly staffed while the remainder 81% feels that IFIs are staffed with competent workers to a certain extent.[472] This indicates the shortage of Islamic finance talents and inadequate development for them to fulfill the shortage.

Obviously, the critical demands on the high-level Islamic finance talents are very crucial. However, the most important for the industry is to get suitable talents to fulfill the need for the Islamic finance industry. The talent shortage issue could be highlighted as follows:

1. The shortage of Islamic finance talents globally in all levels from the *Sharī'ah* officers, *Sharī'ah* scholars and Islamic finance academician.
2. The shortage of *Sharī'ah* scholars with the correct combination of knowledge, especially in Islamic jurisprudence, banking and finance and proper international languages such as English and Arabic to serve in *Sharī'ah* Advisory Committees and worldwide.
3. The issue of "brain drain" among Islamic banking and finance competitors in Malaysia and also the migrating of talent from other Islamic Finance countries, especially from Dubai, Bahrain, Singapore, Hong Kong and London due to more better offers.
4. The need for effective ways to develop Islamic finance experts and high-skilled workers such as job protection, clear career development and promotion, and continuous on- the-job training.

The Islamic finance talents have inter-relations with training, consultancy, education, higher learning, migration and so on. The supply and demand of these talents

http://thestar.com.my/metro/story.asp?file=/2011/9/29/metroperak/9587530&sec=metroperak.

472 Deloitte, The Deloitte Islamic Finance leaders survey in the Middle East: Benchmarking Practices, (United Kingdom: Deloitte and Touch (M.E.), 2011), 31.

could be determined by three major parties, namely the government, the Islamic financial institutions and the individuals. The government endures responsibilities in developing a sound and robust program to build Islamic finance talents such as by designing curriculum, establishing training and educational institutes, formatting labor union policies, dealing with immigrations of talents, harmonizing taxes and providing other related incentives.[473]

Islamic finance industries also face challenges in developing talents. Thus, many Islamic banks send their staff to seminars and other training programs in order to develop their skills and knowledge. However, it is not sufficient to provide Sharī'ah-related knowledge with the expectation to have a well *Sharī'ah* expert staff. A formal education in *Sharī'ah* knowledge is indeed required to understand *Sharī'ah* such as learning Arabic language, Usul Fiqh, Fiqh Muamalat and other related *Sharī'ah* studies.[474]

Currently, many banks opted to approach Sharī'ah-based people in order to have *Sharī'ah* advices. However, such move creates operational issues, where most of them have less knowledge in economy and banking principles. Some of *Sharī'ah* experts made *Sharī'ah* rulings without concerning the impact to the bank's performance and earnings, economic sustainability, consumer related interests and other related operational and technical issues.[475]

Hence, the development of Sharī'ah-trained economists is vital to get the attention of Islamic finance regulators and industry players to ensure that the speedy development of an Islamic finance in the country could be achieved within the schedule. According to the survey administered to industry practitioners and executives Islamic financial leaders of the Middle East Islamic Financial Institutions (IFIs), which was

---

[473] Agil Natt, Syed Othman al-Habshi and Mohd Pisal Zainal, "A Proposed Framework in the Human Capital Development in the Islamic Financial Services Industry," 14.

[474] Saiful Azhar Rosly, *Critical issues on Islamic Banking and Financial Markets: Islamic Economics, Banking and Finance, Investments, Takaful and Financial Planning*, 347.

[475] *Ibid.*

conducted by Deloitte Islamic Financial Knowledge Center (IFKC) in 2011, about 61 percent Islamic Finance staff required more training and skills development and only 18 percent have appropriate training.[476]

The shortage of Sharīʼah-economist talents had raised interest among Malaysian universities to provide enhanced program that consolidates *Sharīʼah* and economic knowledge. Currently, a number of universities in Malaysia offer an undergraduate degree in Islamic banking and finance. Some universities established an Islamic finance faculty - a bigger size compared to a department, where more courses on Islamic banking could be offered, which includes programs like finance, accounting and actuary and together with *Sharīʼah* subject such as Usul Fiqh, Maqasid Sharīʼah, Islamic banking principles and so on. The International University of Islamic Science, Malaysia (USIM) established the Faculty of Economic and Muamalat. This faculty offers four programs for students to choose from; Bachelor of Muamalat Administration, Bachelor of Accounting, Bachelor of Marketing (Financial Services) and Bachelor of Administration and Corporate Admin.

In other long-established Malaysian universities such as University of Malaya and the International Islamic University of Malaysia (IIUM), Islamic banking and finance courses are offered to the students with the combination of subjects such as *Sharīʼah* and Economy. In the University of Malaya, the Islamic Academy Studies offers the *Sharīʼah* and Economic course in both undergraduate and postgraduate levels. At the International Islamic University of Malaysia, Economic students were required to take combination of subjects such as management, Islamic economics, law, Arabic, accountancy, information technology and banking.

[476] Daud Vicary Abdullah (2011), "Growing Islamic Finance: Awareness, Education & Talent Development," (Deloitte -SIDC Islamic Markets Programme 2011 -June,29 2011 –Kuala Lumpur, 2011), 17.

Referring to *Sharī'ah* scholars for *Sharī'ah* advice is compulsory, but for the issue related to finance and banking, the advice must come from a person who has the knowledge of *Sharī'ah* and finance. As such, they understand their ruling's effects on the bank's performance in terms of economic growth, risk, market size and others.

Considering the human capital shortage requires a strategic framework and timeframe for further action. The expectation to solve this issue must be is within a certain timeframe of either in the short-medium or in the long run period. For instance, in the short-term solution, the shortage in human talent can be fulfilled by hiring foreign talents or getting a consultation from the experts with a certain agreed payment. In the medium term, the Islamic finance institution must provide sufficient courses and training to their staff to enhance their skills and competencies. For the long term, better offer and salary increment should be considered for staff retention.

These efforts may involve special offer for employee that consists of job security, benefits, and compensation, which may attract the talent to stay and serve for a long time of period and make the institutions as a place for his career development. Hence, the institutions must play roles to prolong their employees' services with the institutions and at the same time develop their soft skills. [477]

Based on the report, human capital in Islamic finance becomes highly demanded in the Gulf countries in which about 30,000 Islamic finance's personnel are required in the next decade. Assuming the number of executives, which represents 50% of the total number, it means that about 15000 officers are needed. If this calculation includes Indonesia, Pakistan and other Southeast Asian countries, then the amount will raise up to more than 50000.[478] The average calculation shows at least 3,500 trained personnel in Islamic Finance need to be produced every year.[479]

---

[477] Agil Natt, Syed Othman al-Habshi and Mohd Pisal Zainal, "A Proposed Framework in the Human Capital Development in the Islamic Financial Services Industry," 14.
[478] *Ibid*, 20.
[479] *Ibid.*

Therefore, a strategic collaboration among the Malaysian Islamic finance authorities is needed to produce Islamic finance talents. The Islamic finance industries as the user of these talents and the Universities as the factory production must tie a strong co-operation among them to "build" more talents in Islamic finance. Hence, investment from the Islamic finance industries to the universities is somewhat vital to create more Islamic finance officers to fulfill the shortage.[480]

Therefore, as a proposal to resolve the human capital shortage, there are some measures for Islamic finance authorities to be considered as follows:

1. A co-operation network between regulators, academic institutions and industry players to set up a proper framework to develop Islamic Finance talent.
2. Incentives offerings to Islamic Finance related talent to sustain their services.
3. To increase fund for staff training.
4. To co-operate with Islamic finance scholars from other countries in mutual knowledge and experience sharing.
5. Creating awareness of Islamic finance among the public.
6. In increasing domestic Islamic finance expert, a special treatment by the government could be considered for the foreign Islamic finance scholars such as Malaysian permanent residence in order to allow them to serve in Malaysia for a long period.

The development of human talent in Islamic finance must also come together with the frequency of research and study in that field. Research makes things extend and develop. There are many topics of Islamic finance issues to be reviewed such as product development, *Sharī'ah* contracts, legal amendment, and risk management. Research is important for the sustainability of Islamic finance to be continuously available,

[480] Economist Corporate Network, *The Global Outlook of the Islamic Finance Services Industry: An Economist Corporate Network Brief*, (Singapore: The Economist Intelligent Unit Ltd., 2010),13.

competitive and innovative.[481] Hence, measures must be taken among the research institution and together with the industry to provide solutions for any issues in Islamic banking and finance. Research collaboration is important to seek the best view from the convergence of ideas beyond the geographical boundaries.[482]

5.7.1 Analysis and Result

Human talent supply in Islamic finance could be categorized into ordinary and high level talents. Most of the respondents' views the sufficient supply in ordinary talents but not in the high level talents. Hence, a critical shortage of talent in Islamic finance could be defined as a shortage of Islamic finance experts. R5 and R6 viewed the shortage in Islamic finance as the shortage in high-level talent supply. The industry requires very knowledgeable people who have ample knowledge not only in *Sharī'ah*, but also in critical areas like finance and law to consult and advice the IFI such as in product development, *Sharī'ah* compliance matters, and the *Sharī'ah* risk. R5 responded:

> *"There are still shortages in talent supply in Islamic finance. What I mean is a qualified talent and a very well knowledge person in both Sharī'ah and finance knowledge."*

R6 responded on the same question:

> "*......the shortage of talent is the shortage of the expertise."*

R5 insisted the newly approved regulation by BNM called Islamic finance Services Act or IFSA has clearly stipulated the requirement for *Takāful* operators to appoint separate officers in doing underwriting. R5 says:

> *"In addition, the new regulation of Bank Negara Malaysia requires talent to acquire certain certificate to do certain Islamic*

---

481 Zeti Akhtar Aziz, "Talent Development in Islamic Finance Over The Next decade," (Keynote address by
Dr Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia, at the Launching of
IBFIM's Islamic Finance Qualification Framework & Progression Route (IFQFPR), Kuala Lumpur, 14
December 2011).

482 *Ibid.*

Finance task. For instance the underwriting task must be done by a person who own the certificate related to the underwriting. It's mean that one person can't do many task in Takāful. This new policy has steered the increase demand of Islamic finance talent in the long run."

R5 added that the shortage of Islamic finance expert is occurring everywhere and not limited to Malaysia per se:

> *"The shortage is not happens in Malaysia itself, but in the global world. Global Islamic finance has shortage talents in all Islamic finance segment such Sharī'ah expert, Islamic accounting expert and so on so forth."*

In responding to a similar question, R1 viewed that the supply of human talent in Islamic finance must be balanced with the demand in the market. Otherwise, it will result in the over-supply in the market. R1 responded:

> "*The issuance of talents in Islamic finance should be balanced with the existence of the institutions that demand their services. Otherwise, it could cause to over-supply of human talents in Islamic finance."*

R7 viewed that Malaysian talents in Islamic finance are demanded in Arab countries due to their efficiencies and capabilities in completing every task entrusted by the superior. According to R7, a skilled talent could be developed through experience and wide exposure in Islamic banking and finance. A young and fresh graduated Malaysian student from Malaysian higher institutions is described as a well knowledgeable student who meets the industry's requirement. R7 said:

> *"...human Capital in Malaysia .....we are producing people....we are exporting people....ok, in Islamic finance...Alhamdulillah we are doing well....It just needs to be polished more....maybe specifically the expertise ...of course....for instance those who are graduated from IIU or from UM or from Inceif or from any other places, they need to have more skill, I mean that will be acquired through the experience, through their exposure when they work....."*

In sum, Malaysia has successfully produced talents in Islamic finance. Malaysian higher education institutions over the years designed a comprehensive syllabus, which combines Islamic literature and finance. Malaysian universities provide courses in Islamic economics and *Sharī'ah* and different universities use a different name but the combination of the two areas of studies is their primary objective. Hence, students graduated from the universities are capable to understand matters related to *Sharī'ah* and finance. This is evidenced through the demand from Arab countries on Malaysian experts and talents as mentioned by R7.

5.8 CHAPTER SUMMARY

Based on the above study it is obvious that the Central Bank of Malaysia has constantly taken significant measures to develop a comprehensive Islamic banking and finance system in Malaysia. Among the measures are strengthening the Islamic finance regulations, opening more specific Islamic banking and finance education center to provide teaching in Islamic finance like the International Center for Education in Islamic Finance or (INCEIF) and establishing the International *Sharī'ah* Research Academy for Islamic Finance or (ISRA). In the objective to position Malaysia as an Islamic finance global hub, the Central Bank of Malaysia has established Malaysia International Islamic Financial Center (MIFC) with the function to promote Malaysia as an Islamic financial center. It is evidenced through several series of interviews that the Central Bank of Malaysia has successfully designed a successful plan for future development of Islamic banking and finance in Malaysia.

With regard to the issue on the establishment of an Islamic finance court, most of the respondents disagreed on the suggestion of the establishment of an Islamic finance court in the current year due to inadequate cases in the court and technically, most of the cases are about claims from Islamic banks towards the defaulters. Both regulators and practitioners viewed that there is no need for the establishment of an Islamic finance court in the time being.

Most of the respondents agreed on the shortage of Islamic finance talents in the high level such as Islamic finance scholars and well-trained officers. However, this shortage exists everywhere and not only in Malaysia per se, but also in the global Islamic finance countries. The requirement for Islamic finance experts is due to the nature of Islamic banking finance, which requires an approval from Islamic finance scholars such as on new Islamic finance products and issues pertaining to the Islamic finance disputes. In contrast to the conventional finance, the opinions from the scholars are required in order to determine the permissibility of certain contracts based on the evidence from *Sharī'ah*.

Among the critical issues pertaining to the global hub vision is a competition between local and foreign Islamic banking and finance institutions. This is vital to understand that once the government decided to liberalize domestic markets, the existence of foreign contenders could not be eliminated. However, some scholars agree on the view that a security plan must be included in the policy to eliminate local IFIs from any harm as a result of this competition. Hence, some of them view the requirement to limit business model of foreign IFIs is important, for instance to avoid competition with domestic Islamic banks. However, some of them view the positive impact of this competition, which could steer the development of technologies and the increase number of experts. Competition requires each party to provide the best services to the customers and this competition eventually benefits Malaysian clients.

The internationalization of local IFIs is also among the vital issues to be taken into consideration. This is due to the expansion of local IFIs, which indicates the level of strength of the local IFIs. Mostly, the strength of local IFIs is not only accounted from their capability to compete in the home market, but also outside the country. The expansion will benefit the IFIs in terms of new market exposure, more clients, strategic future plans to grab foreign market and as a catalyst to appear as a global player in the global market.

An idea of an Islamic Megabank is brilliant to complement the vision of becoming an Islamic finance global hub. However, its existence must be clearly defined as a bank with a huge capital, which makes its presence everywhere in the global Islamic finance countries, and not only serve inside the country. Of course, certain limitations regarding the client base must not be similar to domestic IFIs as it might affect local IFIs in which the bigger IFI normally wins the competition.

As a conclusion, it is worth to note that the issues discussed in this chapter are important to be highlighted in this study as most issues appear in the current real Islamic finance global hub scenario in Malaysia. A comparative analysis of scholars' views resulted in the safe decision to opt for the better choice of the overall views and opinions, which would provide better solution of the issue.

CHAPTER 6

ANALYSIS ON THE GLOBAL ECONOMIC ASSESSMENT BODIES AND A PROPOSAL FOR A NEW FRAMEWORK FOR ISLAMIC FINANCE GLOBAL HUB INDEX

6.0 INTRODUCTION

This chapter attempts to observe the credible assessment bodies around the world in assessing country's economic performance as well as in evaluating the global financial hub countries. Based on the literature review, this study concludes three assessment bodies as a sample for a comparative analysis to explore their methods in assessing a country's economic performance. The ultimate objective from this comparative analysis is to develop a new index that can be used to assess the Islamic finance global hub. Hence, the exploration on the three assessment bodies is important to conclude the appropriate method to be included in the new index. Overall, this chapter answers the fourth research question as pointed in problem statement in the first chapter of this thesis.

The three assessment bodies selected as samples in this study are as follows:

1. The Global Competitiveness Report
2. The Global Financial Center Index
3. Ernst & Young (E&Y) Globalization Index

The development of the new index for Islamic finance global hub assessment requires validation from regulators and experts in Islamic finance. Therefore, this study applied a mix method, which consists of survey and interview methods in order to ensure the reliability of the index.

A survey method was conducted to seek views from respondents working in the department of Islamic banking and Takaful at the Central Bank of Malaysia. Several variables were developed with descriptions embedded in each variable. These variables were included in a set of survey form and distributed among the staff. To access the content validity scales related to the questionnaire survey, three experts rated the questionnaire items as explained in the first chapter. The data were analyzed using SPSS. Descriptive analyses were used to determine the degree of each variable in the index. Accordingly, changes were made to the first draft by eliminating, adding to or rewording some of the questions included in the draft. The revised questionnaire was distributed throughout November 2014 – January 2015. The questionnaires were distributed using self-administered method.

The 5-point of Likert scale questionnaire that was developed covers the subjects and descriptions of the Islamic finance global hub index. The second section of the questionnaire comprises items to obtain demographic information and the third section contains the appendix. The first section consists of 30 different questions. The 5-point Likert scale includes “Strongly Disagree,” “Disagree,” “Neutral,” “Agree,” and “Strongly Agree.”

The unit of analysis involves in this study as detailed in chapter one consist of three groups namely regulator, banker and researcher.

There are ten variables covered under the survey, namely the *Islamic Finance Regulation and Supervision, Islamic Finance Talents, Islamic Finance Shares and Quantities, Islamic Finance Sectors, Taxation, Environment Support, Cost, Access, Liberalization Policy* and *Category: National, Regional, International and Global Hub.*

An interview method was conducted among Islamic finance scholars. Two prominent Islamic finance scholars agreed to review the framework, namely Prof. Dr. Mohamad Akram Laldin who was tagged as R7 and Assoc. Prof. Dr. Lahsasna Ahcene, tagged as R6. The details of both respondents are presented in the previous chapter. The interview procedures began from the preparation of semi structured interview questions until the analysis of the interview data. During the interview, some of the variables were accepted by the respondents and vice versa. Therefore, in some variables, no comments presented from both respondents. Hence, in explaining some variables, there is only the explanation of mean analysis without comments from both respondents, which indicates that they agreed with the variable and its description.

In other variables, the explanation of the result and the scored number are embedded in each variable with additional comments from the Islamic finance scholars. The explanation of the result is presented using the mean analysis method.

6.1 COMPARATIVE ANALYSIS BETWEEN THE GLOBAL ECONOMIC INDEX

Based on the cumulative readings and evaluation on the financial center reports and indexes, there are three international and recognized assessment bodies, which provide assessment on the global economic performance. The following assessment bodies are:

1. The Global Competitiveness Report
2. The Global Financial Center Index
3. Ernst & Young (E&Y) Globalization Index 2011

The selection of the three assessment bodies was made in accordance to their effective reports towards global economies. Although the result of each assessment body is different, this is not an issue because the aim of this study was to observe the applied method in the three assessment bodies.

6.1.1 Evaluation by the Global Competitiveness Report

6.1.1.1 Historical Background

The Global Competitiveness Report (GCR) is published by the World Economic Forum based on its annual observation on the global economic performance. Historically, the World Economic Forum (WEF) is a non-profit organization based in Geneva, Switzerland and was founded in 1971.[483] The Forum functions as a catalyst for the world dialogues in improving political, economic and social awareness as well as acting as a platform for major bridge-building efforts. Another function of WEF is to provide a critical platform for the peace, stabilization and reconciliation in many countries around the world.

The *Global Competitiveness Report 2014-2015* assesses the competitiveness landscape of 144 economies, providing insight into the drivers of their productivity and prosperity. The report remains the most comprehensive assessment of national competitiveness worldwide; providing a platform for dialogue between government, business and civil society about the actions required to improve economic prosperity. Competitiveness is defined as *the set of institutions, policies and factors that determine the level of productivity of a country*. The level of productivity, in turn, sets the level of prosperity that can be earned by an economy. [484]

The different aspects of competitiveness are captured in 12 pillars, which compose the Global Competitiveness Index. This 35th edition emphasizes innovation and skills as the key drivers of economic growth. While these increasingly influence competitiveness, the global economy tentatively recovers from the economic crisis,

---

[483] Official website of the World Economic Forum, "History", retrieved on 26 December 2013, http://www.weforum.org/history.

[484] Official website of the World Economic Forum, "Reports", retrieved on 22 Jun 2015, http://www.weforum.org/reports/global-competitiveness-report-2014-2015.

significant risks remain, resulting from a strained geopolitical situation, rising income inequality and the potential tightening of financial conditions. It is, therefore, crucial to address these structural challenges to ensure more sustainable and inclusive growth. More than ever, cooperative leadership among business, government and civil society is needed to re-establish sustainable growth and raise living standards throughout the world.[485]

6.1.1.2 Evaluation Method:

The computation of the GCI is based on successive aggregations of scores from the indicator level (i.e., the most disaggregated level) all the way up to the overall GCI score. Unless noted otherwise, GCI uses an arithmetic mean to aggregate individual indicators within a category.

The Survey is divided into 14 sections:

I. About Your Company
II. Overall Perceptions of Your Economy
III. Infrastructure
IV. Innovation and Technology Infrastructure
V. Financial Environment
VI. Foreign Trade and Investment
VII. Domestic Competition
VIII. Company Operations and Strategy
IX. Government and Public Institutions
X. Education and Human Capital
XI. Corruption, Ethics and Social
XII. Responsibility
XIII. Travel & Tourism

[485] *Ibid.*

XIV. Environment

XV. Health

For the higher aggregation levels, the GCI uses the percentage shown next to each category. This percentage represents the category's weight within its immediate parent category. Reported percentages are rounded to the nearest integer, but exact figures are used in the calculation of the GCI. For example, the score a country achieves in the 11th pillar accounts for 50 percent of this country's score in the innovation and sophistication factors' subindex, irrespective of the country's stage of development. Similarly, the score achieved on the transport infrastructure subpillar accounts for 50 percent of the score of the infrastructure pillar. Unlike the case for the lower levels of aggregation, the weight put on each of the three subindexes (basic requirements, efficiency enhancers, and innovation and sophistication factors) is not fixed. Instead, it depends on each country's stage of development, as discussed in the chapter.

For instance, in the case of Burundi—a country in the first stage of development—the score in the basic requirements subindex accounts for 60 percent of its overall GCI score, while it represents only 20 percent of the overall GCI score of Sweden, a country in the third stage of development. For countries in transition between stages, the weighting applied to each subindex is reported in the corresponding profile at the end of this volume. For instance, in the case of Azerbaijan, currently in transition from stage 1 to stage 2, the weight on each subindex is 56.3 percent, 37.8 percent, and 5.9 percent respectively..[486]

6.1.1.3 Countries Position in the Global Competitiveness Index 2013-2014

[486] *Ibid.,* 49.

Table 6.1: The Global Competitiveness Index 2013-2014 Rankings and 2014-2015 Comparisons:[487]

Country/Economy	GCI 2014 – 2015		GCI 2013-2014
	Rank	Score	Rank
Switzerland	1	5.70	1
Singapore	2	5.65	2
United States	3	5.54	3
Finland	4	5.50	4
Germany	5	5.49	5
Japan	6	5.47	6
Hong Kong SAR	7	5.46	7
Netherlands	8	5.45	8
United Kingdom	9	5.41	9
Sweden	10	5.41	10

Source:http://reports.weforum.org/global-competitiveness-report-2014-2015/wp-content/blogs.dir/54/mp/files/pages/files/tables3-7-wef-globalcompetitivenessreport-2014-15-2.pdf

6.1.1.4 Factors of Evaluation

This evaluation included several factors of key measurement in assessing the economic performance in the country. The factors are named as pillars. The following pillars are listed as follows:

1. Institutions
2. Infrastructure
3. Macroeconomic Environment
4. Health and Primary Education
5. Higher Education and Training
6. Goods Market Efficiency
7. Labor Market Efficiency

[487] *Ibid.*

8. Financial Market Development
9. Technological Readiness
10. Market Size
11. Business Sophistication
12. Innovation

As a conclusion from the above, it could be summarized that the World Economic Forum functions to provide data regarding a country's competitiveness. The report also provides the strong sectors, which strengthen the economic performance together with the recommendation on the improvement of other sectors.

The following table presents the details of the global competitiveness report evaluation program:

Table 6.2: Summary of the Global Competitiveness Report

Name of Organizer	The World Economic Forum, based in Geneva, Switzerland.
Name of Program	The Global Competitiveness Report 2014-2015
Method of Evaluation	Survey Questionnaire and the data analyzed using mean arithmetic
Factors of Evaluation	1. Institutions 2. Infrastructure 3. Macroeconomic Environment 4. Health and Primary Education 5. Higher Education and Training 6. Goods Market Efficiency 7. Labor Market Efficiency 8. Financial Market Development 9. Technological Readiness 10. Market Size 11. Business Sophistication 12. Innovation

6.1.2 Evaluation by the Global Financial Center Index III

6.1.2.1 Historical Background

In March 2007, Z/Yen Group published the first issuance of the Global Financial Center Index. This effort is taken subsequence to another project into city competitiveness conducted by Z/Yen Group in 2005. The prime objective of the GFCI is to analyze the major financial centres globally in terms of competitiveness. The frequent of publication is once in every six months (although the index is actually produced every three months).[488] The GFCI provides profiles, ratings and rankings over 75 financial centres drawing on two separate sources of data – instrumental factors (external indices) and responses to an online survey.[489]

The GFCI provides ratings for financial centres calculated by a 'factor assessment model' built using two distinct sets of input:[490]

Instrumental factors (external indices that contribute to competitiveness): Objective evidence of competitiveness was sought from a wide variety of comparable sources. For example, evidence about the infrastructure competitiveness of a financial centre was drawn from a survey of property and an index of occupancy costs. Evidence about a fair and just business environment is drawn from a corruption perception index and an opacity index. A total of 64 external sources were used in GFCI 7. Not all financial centres are represented in all the external sources, and the statistical model takes account of these gaps.[491]

---

[488] Long Finance of Z/Yen Group, *The Global Financial Centres Index 10*, (Qatar: Long Finance, 2011), 2.
[489] *Ibid.*
[490] (In 2007 Z/Yen and a group of interested and motivated individuals launched the Long Finance initiative. The aim is to promote discussion, research and education about finance).
[491] Long Finance of Z/Yen Group, *The Global Financial Centres Index 10*, 32.

6.1.2.2 Evaluation Method

The GFCI provides ratings for financial centres calculated by a 'factor assessment model' that uses two distinct sets of input:

• Instrumental factors: objective evidence of competitiveness was sought from a wide variety of comparable sources. For example, evidence about the telecommunications infrastructure competitiveness of a financial centre was drawn from a global digital economy ranking (supplied by the Economist Intelligence Unit), a telecommunication infrastructure index (by the United Nations) and a Global Information Technology Index (by the World Economic Forum). Evidence about a business-friendly regulatory environment is drawn from the Ease of Doing Business Index (supplied by the World Bank) and an Institutional Effectiveness rating (from the EIU) amongst others. A total of 105 instrumental factors are used in GFCI 17 (of which 36 were updated since the GFCI 16 and 10 are new to the GFCI). Not all financial centres are presented in all the external sources and the statistical model takes account of these gaps.[492]

• Financial centre assessments: by means of an online questionnaire, running continuously since 2007, we used 28,494 financial centre assessments drawn from 3,527 respondents in GFCI 17.[493]

A centre is only given a GFCI rating and ranking if it receives more than 200 assessments from other centres within the previous 24 months in the online survey. Centres in the GFCI that do not receive 100 assessments in a 24 month period are removed and added to the Associate list until the number of assessments increases.

The financial centre assessments and instrumental factors are used to build a predictive model of centre competitiveness using a support vector machine (SVM). SVMs are based upon statistical techniques that classify and model complex historic data in order to make predictions of new data. SVMs not only work well on discrete,

---

[492] Long Finance of Z/Yen Group, *The Global Financial Centres Index 10*, (Qatar: Long Finance, 2015), 43.
[493] *Ibid.,* 44.

categorical data, but also handle continuous numerical or time series data. The SVM used for the GFCI provides information about the confidence with which each specific classification is made and the likelihood of other possible classifications.[494]

6.1.2.3 Factors of Evaluation

1. Business Environment factors
    a. Political Stability and Rule of Law
    b. Institutional and Regulatory Environment
    c. Macroeconomic Environment
    d. Tax and Cost Competitiveness
2. Financial Sector Development
    a. Volume and Velocity of Trading
    b. Availability of Capital
    c. Depth and Breadth of Industry Clusters
    d. Employment and Economic Output
3. Infrastructure Factors
    a. Building and Office Infrastructure
    b. Transport Infrastructure
    c. ICT Infrastructure
    d. Environmental Care and Sustainability
4. Human Capital
    a. Availability of Skilled Personnel
    b. Education and Development
    c. Flexible Labour Market and Practices
    d. Quality of Life
5. Reputational and General Factors
    a. City Brand and Appeal
    b. Level of Innovation
    c. Attractiveness and Cultural Diversity

[494] *Ibid.*

d. Comparative Positioning with Other Centers

6.1.2.4 Top 10 Countries' Position in The Global Financial Centre Index (GFCI) Ranking

Table 6.3: The list of the top ten countries in GFCI.

Center	GFCI 17		GFCI 16		CHANGES	
	Rank	Rating	Rank	Rating	Rank	Rating
New York	1	785	1	778	-	+ 7
London	2	784	2	777	-	+ 7
Hong Kong	3	758	3	756	-	+ 2
Singapore	4	754	4	746	-	+ 8
Tokyo	5	722	6	718	+ 1	+ 4
Zurich	6	719	7	717	+ 1	+ 2
Seoul	7	718	8	715	+1	+ 2
San Francisco	8	708	5	719	-3	-11
Chicago	9	707	12	702	+ 3	+ 5
Boston	10	706	9	705	-1	+ 1

Source: Countries position in The Global Financial Centre Index (GFCI) 17 (March 2015)

Table 6.4: Summary of Global Financial Center Index (GFCI)

Name of Organizer	Z/ Yen Group
Name of Program	The Global Financial Centre Index (GFCI)
Date of Establishment	The Global Financial Center Index was first published in March 2007 following another research project into city competitiveness undertaken by Z/Yen Group in 2005.
Evaluation Method	Survey Questionnaire method and the data analyzed using the support vector machine (SVM).
Factor of evaluation	1. Business Environment factors a. Political Stability and Rule of Law b. Institutional and Regulatory Environment c. Macroeconomic Environment d. Tax and Cost Competitiveness 2. Financial Sector Development a. Volume and Velocity of Trading b. Availability of Capital c. Depth and Breadth of Industry Clusters d. Employment and Economic Output 3. Infrastructure Factors a. Building and Office Infrastructure b. Transport Infrastructure c. ICT Infrastructure

	d. Environmental Care and Sustainability 4. Human Capital a. Availability of Skilled Personnel b. Education and Development c. Flexible Labour Market and Practices d. Quality of Life 5. Reputational and General Factors a. City Brand and Appeal b. Level of Innovation c. Attractiveness and Cultural Diversity d. Comparative Positioning with Other Centers
Number of issuances	The GFCI has issued indexes up to 17 issuances starting from 2007 and the latest had been issued recently in March 2015.

6.1.3 Evaluation by Ernst & Young (E&Y) Globalisation Index 2011

6.1.3.1 Historical Background

EY's annual Globalization Index was first developed in 2009 in conjunction with the Economist Intelligence Unit. The Index is based on a comprehensive understanding of the underlying drivers for globalization across five main pillars: openness to trade, capital flows, exchange of technology and ideas, labor movements, and cultural integration. With these key categories, the Index incorporates a broad range of sub-indicators for 60 countries and spans a 20-year time horizon from 1995 to 2016.
As globalization evolves and new and better data sets become available, it is appropriate to review the index data and methodology to accurately reflect these developments. In 2012 there is a revision introduced to the Globalization Index scoring system and several new sub-indicators are included to better reflect the state of play in the global economy, technology and markets.[495]

6.1.3.2 Evaluation Method

[495] http://www.ey.com/GL/en/Issues/Driving-growth/Globalization---Looking-beyond-the-obvious---2012-Index

The Index covers 60 countries around the world, whereby the measurement is based on the GDP. The new scoring system uses a dynamic normalization technique. In addition, the following variables are included in the 2012 Index:

- Share of main trading partners in total trade, as a percentage of GDP (trade in goods and services)
- Trade in information and communications technology (ICT) goods as a percentage of GDP (technology)
- Foreign direct investment (FDI) stocks as a percentage of GDP (capital and finance)
- Total international fixed telephone traffic (culture)

The last two of these variables are substitutions for the FDI flows as a percentage of GDP (capital and finance) and international outgoing fixed telephone traffic (culture). The sub-indicator weights in the index have been redistributed to reflect the changes in the variables.[496]

The purpose of these changes is to better capture a country's relative performance and performance over time across the five main drivers of globalization. The changes are reflected in some larger-than-normal historical revisions to the 2011 ranking, but the updated Index methodology can better capture the nuances in globalization in the world today, suggesting improved forecasting capability and insights into key business opportunities and challenges.

6.1.3.3 Factors of Evaluation

[496] http://www.ey.com/GL/en/Issues/Driving-growth/Globalization---Looking-beyond-the-obvious---2012-Index.

The following items are the factors included in the evaluation:

1. Movement of Goods and Services (22%)

a. Total trade (Exports and Imports)

b. Trade Openness

c. Tariff and Non-Tariff Barriers

d. Ease of Trading (Cross-Border)

e. Current-account Restrictions

f. Share of Main Trading Partners in Total Trade

2. Movement of Capital and Finance (21%)

a. FDI stocks (in and out, % GDP)

b. Portfolio Capital Flows (in and out, % GDP)

c. Government Policy towards Foreign Investment

d. Expropriation risk

e. Investment Protection Schemes

f. Domestic Favoritism by Government

g. State Control/ Ownership

3. Exchange of Technology and Ideas (21 %)

a. Trade in ICT goods (exports and imports) as % of GDP

b. Broadband Subscriptions (per 100 people)

c. Internet subscribers (per 100 people).

4. Movement of Labor (19 %)

a. Net Migration rate (per 1000 population)

b. Current Transfer (in and out, as % GDP)

c. Hiring of Foreign Nationals

5. Cultural Integration (17%)

a. Tourism (in and out, per 1000 population)

b. International total fixed telephone traffic (minutes) per capita

c. Openness of national culture to foreign influence

6.1.3.4 Countries' position in Ernst & Young (E&Y) Globalization Index 2012

Table 6.5: List of the top ten countries in Ernst & Young (E&Y) Globalization Index 2012

Country	Rank	2012 Score	Change in Score Since 2011
Hong Kong	1	7.81	0.06
Singapore	2	6.31	- 0.02
Ireland	3	5.63	0.08
Belgium	4	5.49	0.11
Switzerland	5	5.30	0.04
Netherland	6	5.19	0.02
Sweden	7	4.96	0.01
Denmark	8	4.94	0.01
Hungary	9	4.75.	0.07
United Kingdom	10	4.74	0.03

Source: Ernst & Young Globalization Index 2012

The following table detailed the Ernst & Young Globalization Index evaluation program:

Table 6.6: Summary of Ernst & Young (E&Y) globalization Index

Name of Organizer	Ernst & Young (E&Y)
Name of Program	Ernst & Young (E&Y) Globalization Index.
Evaluation Method	The Globalization Index measures the countries by GDP as well as forecast four years ahead of GDP's performance. (The Index measure "relative" rather than "absolute" globalization. This means that an economy's trade, investment, technology, labor and cultural integration with other economies is measured relative to its GDP rather than by the absolute value of these elements being exchanged).
Factors of Evaluation	1. **Movement of Goods and Services (22%)** a. Total trade (Exports and Imports) b. Trade Openness c. Tariff and Non-Tariff Barriers d. Ease of Trading (Cross-Border) e. Current-account Restrictions f. Share of Main Trading Partners in Total Trade **2. Movement of Capital and Finance (21%)** a. FDI stocks (in and out, % GDP) b. Portfolio Capital Flows (in and out, % GDP) c. Government Policy towards Foreign Investment d. Expropriation risk e. Investment Protection Schemes f. Domestic Favoritism by Government g. State Control/ Ownership **3. Exchange of Technology and Ideas (21 %)** a. Trade in ICT goods (exports and imports) as % of GDP

	b. Broadband Subscriptions (per 100 people) c. Internet subscribers (per 100 people). **4. Movement of Labor (19 %)** a. Net Migration rate (per 1000 population) b. Current Transfer (in and out, as % GDP) c. Hiring of Foreign Nationals **5. Cultural Integration (17%)** a. Tourism (in and out, per 1000 population) b. International total fixed telephone traffic (minutes) per capita c. Openness of national culture to foreign influence

6.2 COMPARATIVE ANALYSIS

6.2.1 Comparative Study on the Three Assessment Bodies

The three assessment bodies, namely the Global Competitiveness Report, the Global Financial Centre Index (GFCI) and the Ernst and Young Global Index, apply different method in evaluating the economic performance in the countries around the world.

Table 6.7: Comparison of the three assessment bodies:

	The Global Competitiveness Report	**Global Financial Center Index (GFCI)**	**Ernst & Young**
Evaluation Method	Survey Questionnaire Method.	Survey Questionnaire method and the data analyzed using the support vector machine (SVM).	The Globalization Index measures the countries by GDP as well as forecast four years ahead of GDP's performance.
Factors of Evaluation	1. Institutions 2. Infrastructure 3. Macroeconomic Environment 4. Health and Primary Education 5. Higher Education and training 6. Goods Market Efficiency 7. Labor Market Efficiency 8. Financial Market Development 9. Technological Readiness 10. Market Size 11. Business Sophistication 12. Innovation	1. Business Environment factors 2. Financial Sector Development 3. Infrastructure Factors 4. Human Capital 5. Reputational and General Factors	1. Movement of Goods and Services 2. Movement of Capital and Finance 3. Exchange of Technology and Ideas 4. Movement of Labor 5. Cultural Integration

Top 10 Countries within the Ranking	1. Switzerland 2. Singapore 3. United States 4. Finland 5. Germany 6. Japan 7. Hong Kong SAR 8. Netherlands 9. United Kingdom 10. Switzerland	1. New York 2. London 3. Hong Kong 4. Singapore 5. Tokyo 6. Zurich 7. Seoul 8. San Francisco 9. Chicago 10. Boston	1. Hong Kong 2. Singapore 3. Ireland 4. Belgium 5. Switzerland 6. Netherland 7. Sweden 8. Denmark 9. Hungary 10. United Kingdom

Each assessment body applies a different method of evaluation. However, in term of factors of evaluation, the same factors are likely adopted in the assessment. For instance, the availability of infrastructure which comprises the access and networking facilities, the advance of IT system, the culture support, the availability of human resource and labor, the efficiency of the system, the business environment which includes political and economic stability and so forth. The differences may be in terms of categorizing the factors using either the inductive or deductive methods.

The Global competitiveness report and the Ernst & Young globalization index evaluate the country as their item of evaluation. However, the Global Financial Center Index used to evaluate financial center as a focus of their evaluation. There is a country that functions both as a country and financial center at the same time such as Singapore. Hong Kong is also ranked in three assessment bodies, which is correct to be considered as a financial center in the GFCI, but it is also included in the evaluation by the Global Competitiveness report and Ernst & Young globalization index. Hence, it could be concluded that the GCR and E & Y Globalization Index used the same sample of evaluation, namely country whilst the GFCI used to evaluate the financial center as the sample of evaluation.

In term of the method used in gathering the data, both GCI and GFCI used the same method, namely a survey questionnaire whilst the E & Y Globalization Index used the GDP report in assessing the index.

6.2.2 Recommendations for Islamic Finance Global Hub Index

From the above observation, this study would like to suggest that in evaluating Islamic financial centres, there should be a special condition embarked in the index items, which have Islamic values. This is vital due to the Islamic financial system, which is based on *Sharī'ah* requirement. For instance, the Islamic financial system prohibits non-Halal transactions in its business. It is unusual if one country with non-Halal transaction such as a country promoting gambling, pork business and prostitution being promoted as the top Islamic financial centres. Therefore, the additional *Sharī'ah* assessment value should be added in evaluating the Islamic financial center global hub country. With remaining current value of evaluation such as the regulatory environment, the access to international financial markets and so on, the additional *Sharī'ah* value will determine the most eligible Islamic financial centre global hub.

Thus, a new interpretation of Islamic financial centre must also be determined since the Islamic finance is different compare to its conventional counterparts. This interpretation will also lead to the accurate evaluation of the Islamic financial global hub. The non-Islamic financial centres such as London, New York and Singapore will also be included in the evaluation, but with the requirement of *Sharī'ah* value. This value is important in assessing the accurate Islamic financial centres and how the financial centre manages Halal and non-Halal business. Although, Malaysia is a country that has gambling and non-Halal business due to its mix cultural citizens, the transaction to non- Halal business will not be approved when using Islamic banking facilities for instance the Islamic credit card will be blocked by the financial provider once it is used in non-Halal transaction. This shows the management of Halal and non-Halal transactions.

Saudi Arabia is another example of a country in which the Islamic and *Sharī'ah* rules could be best implemented. However, the assessment will also include the investor's friendly value, the regulation and tax incentives and others. Therefore, the new Islamic financial centre's evaluation must combine good governance factor and the *Sharī'ah* value at the same time. Hence, the assessment will take into account all the cited factors for the thorough and fair measurement.

This study suggests that the framework of *Sharī'ah* assessment should comprise the following criteria:

1. A strong *Sharī'ah* supervision control to ensure all Islamic finance Institutions comply with *Sharī'ah*. For instance, the control on Islamic credit card usage, which is applicable only in Halal premises.
2. The establishment of *Sharī'ah* court for the settlement of Islamic finance dispute, which is vital to ensure the case hearing in the best manner with suffice of Islamic finance knowledge among the judges, the advocates and all the involved parties.
3. Sufficient *Sharī'ah* compliant products in Islamic banking, Takaful and Islamic capital market.
4. Good asset liquidity management to ensure Islamic finance fund does not leak into non-Halal business.
5. Strong Islamic finance applications include Islamic banking, Islamic Capital Market and Islamic Insurance.
6. A huge number of Islamic finance shares in the economy provides well acceptance among peoples.

6.3 PROPOSAL FRAMEWORK OF ISLAMIC FINANCE GLOBAL HUB INDEX

6.3.1 A Proposal for a new Interpretation of Islamic Finance Global Hub

Based on a previous study, it could be concluded that a new interpretation to the Islamic Finance Global Hub must be addressed in order to clarify the meaning of Islamic finance global hub. Based on the previous study conducted in chapter three, therefore, this study suggests to define the Islamic finance Global Hub as "A country becomes as a hub for local and global financial providers when they offer Islamic finance services that comprises of Islamic banking, takaful and Islamic financial market for the country's residents and International customers."

The interpretation of the Islamic finance global hub is important to drive the concept of Islamic finance global hub framework, which must always comply with the Islamic rules and spirit accordingly.

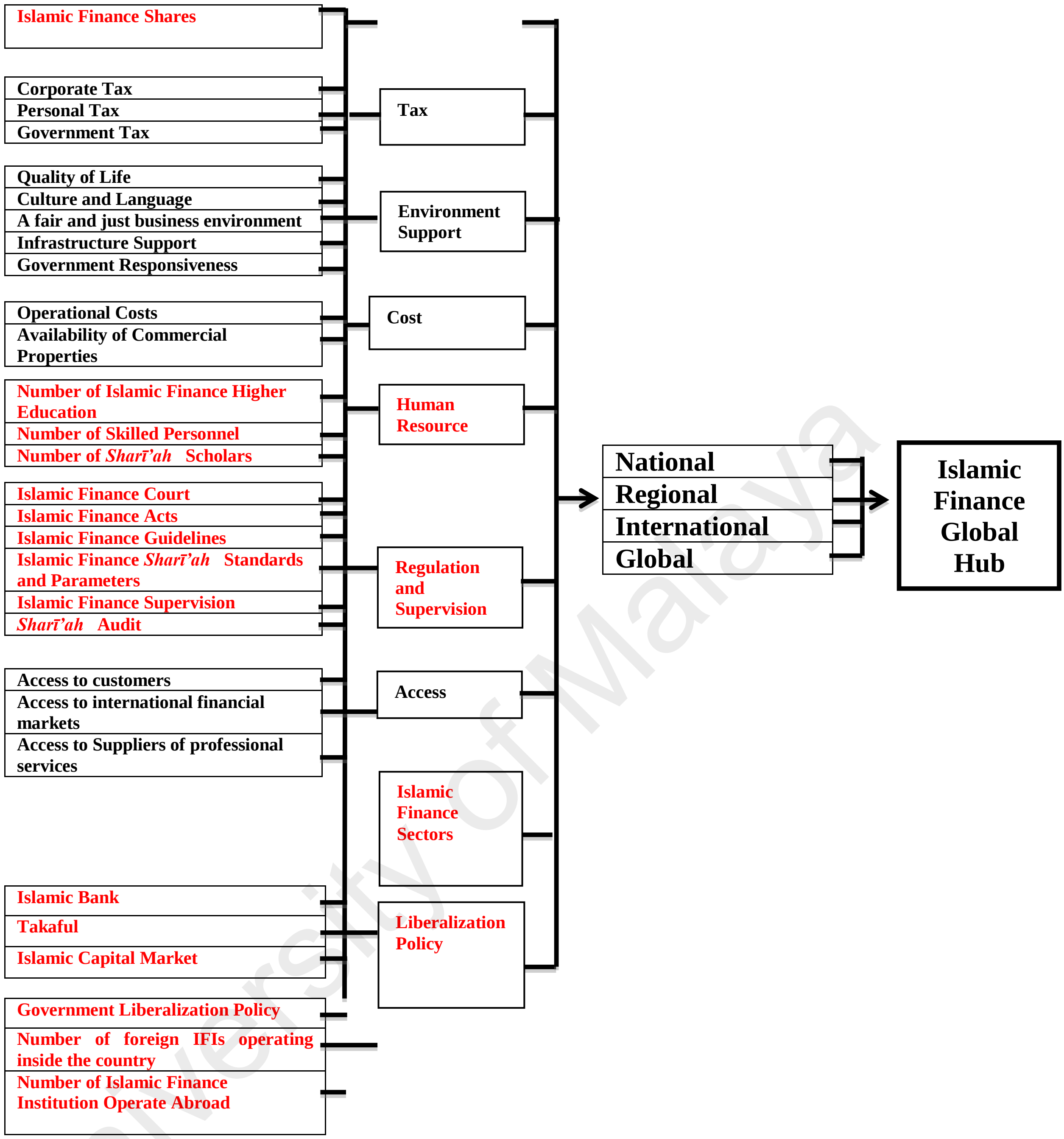
6.3.2 A Proposal Framework for the Islamic Finance Global Hub Index

This proposal consists of the following items:

1. Diagram of the Islamic Finance Global Hub Index.
2. Description of Each Assessment Item
3. Description of the National. Regional, International and Global Hub of Islamic financial country

The Islamic Finance Global Hub Index is inspired by the study conducted from the above analysis. Some of the subjects and items applied by the three assessment bodies, namely the Global Competitiveness Report, the Ernst and Young report and the Global Financial centre Index are adopted to form this new Islamic Finance Global Hub Index Framework with new Islamic elements inserted in this framework, which is highlighted in red.

Diagram 6.1: Islamic Finance Global Hub Framework



#The red colour indicates the new factors added in the framework.

6.3.3 Description of Each Item in the Index

Table 6.8: Description of Each Assessment Subjects

Item	Description
Shares and Quantities	
Islamic Finance Shares	To identify Islamic finance Shares in the country, which will indicate the strength of Islamic finance institutions in term of demand, size and performance.
Number of foreign Islamic finance Institution Operate in the country	To observe the policy of the government in terms of liberalization policy to position the country as the world Islamic finance service provider.
Number of Islamic Finance Institution Operate Abroad	To identify the performance of local Islamic finance institutions in order to determine the efficiency, sustainability, competency and International standard services.
TAX	
Corporate Tax, Personal Tax, Government Tax and Other Related Taxes	Transparency, clarity, simplicity and predictability are vital to be observed regarding to the tax matter.
Environment Support	
Quality of Life	Standard and quality of living promote pleasant working environment and peace of mind.
Culture and Language	Multilingual and good cultures of populations are among important factor of country's internationalization policy.
A fair and just business environment	A fair and just business environment will ensure sound competition, fair legal decision and give the right to the entitled parties.
Infrastructure Support	To determine the availability of infrastructure support such as ICT speed and security, Electricity and water supply, highway networks and connections and other related infrastructure.
Government Responsiveness	The government plays an important role in developing sound domestic business through the affective regulation, tax reduction and fast responsive towards claims and corrections.
Cost	
Operational Costs	The operational cost is important to be included in the assessment as this will determine the capability of the Islamic financial institutions to operate within the appropriate cost.
Availability of Commercial Properties	The availability of commercial properties in the city country will promote the presence of foreign Islamic financial institutions to open the business inside the country.
Human Resources	
Number of Islamic Finance Higher Education	The existence of number of higher education/ learning will promote the issuance of many human capital sources, and hence, will provide the institutions variety of options in choosing the most suitable staff.
Number of *Sharī'ah* Scholars	*Sharī'ah* scholars play a very important role in Islamic finance as they function to approve Islamic finance products and policies, to provide *Sharī'ah* opinions and to clarify any ambiguity in Islamic finance.
Regulation and Supervision	
Islamic Finance Court	The establishment of Islamic finance court is important in the Islamic finance system to function as an arbitrator for the Islamic finance disputes.
Islamic Finance Acts	The sound, affective and robust acts' framework will ensure the efficiency of the Islamic financial system.
Islamic Finance Guidelines	The issuance of Islamic finance guidelines will ease the function of the system.
***Sharī'ah* Standards in Islamic finance**	*Sharī'ah* standard in Islamic finance is important to streamline various *Sharī'ah* interpretations and rulings in Islamic finance.
Islamic Finance Supervision and audit	Islamic finance system is also exposed to the abuse action and wrongdoing from any person who will put the system incompliance with *Sharī'ah* . Thus, the supervision will ensure any mistake is fixed and replaced into the right order.
Access	
Access to customers	Access to customers means physical proximity to clients.
Access to international financial markets	Refers to the IFI's networking with international players to facilitate cross border transaction.

Access to Suppliers of professional services	To observe the availability of professional services such as IT specialist, Expert Accountants both personal and firms, and Legal Firms.

6.3.4 Description of the National, Regional, International and Global Hub of Islamic financial country

Table 6.9: Description of the National. Regional, International and Global Hub of Islamic financial country

National Islamic Financial Country	A country that conducts Islamic financial services within National level. The Islamic financial institutions operate inside the country and there are no licences opened to the foreign Islamic financial Institutions to operate inside the country.
Regional Islamic financial Country	Are defined as a country that provides Islamic financial services within the regional areas. Islamic financial Institutions operate businesses within the region and there are also licences opened to the regional Islamic financial Institutions.
International Islamic financial Country	Refers to a country where the Islamic financial institutions operate in the International level. The country also open licences for foreign Islamic financial centres to operate inside the country. A large volume of cross-border transactions is conducted, whereby these transactions include at least two locations in different jurisdictions.
Islamic Finance Global Hub Country	The most integrated places for Islamic financial services institutions to connect international, national and regional financial services participants directly.

6.4 ANALYSIS AND RESULT

6.4.1 Validity and Reliability of Variables

6.4.1.1 Validity

In order to measure the validity, this study applied expert reviews method. The reviewers comprise of three prominent experts, namely Prof. Dr. Abdul Rahim Abdul Rahman,[497] Prof. Dr. Zainal Abidin Bin Mohamed[498] and Dr. Nuradli Ridzwan Shah Bin Mohd Dali.[499] These personalities are experts in Islamic banking and finance and have a huge experience in the related field. Three sets of survey materials were distributed to all reviewers whereby comments pertaining to the framework of Islamic

[497] Prof. Dr. Abdul Rahim Abdul Rahman is currently a Professor and attached to the Faculty of Economics and Muamalat, the Islamic Science University of Malaysia (USIM) based in Nilai, Malaysia. Beside full-time lecturing at USIM, he is also attached to the International Shari'ah Research Academy in Islamic Finance (ISRA) based in Petaling Jaya, Malaysia, as a Research Fellow.

[498] Prof. Dr. Zainal Abidin Bin Mohamed, is currently a Professor and works at the Faculty of Economics and Muamalat, the Islamic Science University of Malaysia (USIM) based in Nilai, Malaysia. His current position is as the deputy dean of Graduate School of Muamalat in the Faculty of Muamalat, USIM.

[499] Dr. Nuradli Ridzwan Shah Bin Mohd Dali, is a senior lecturer in the Faculty of Muamalat, Islamic Science University of Malaysia.

finance global hub were proposed. Several amendments have been made based on these comments.

6.4.1.2 Reliability of the Measure

Table 6.10: Cronbach's Alpha Result

Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.941	.945	30

The reliability of the variables in the survey was measured by using Cronbach's alpha, which provides reliability of different variables. Based on the standard practice of measurement, when the coefficient is equal or greater than 0.7, the reliability could be considered as acceptable. As shown in the above table, the reliability of Islamic finance index is 0.941, which is greater than 0.7, indicating that all variables are reliable.

6.4.1.3 Mean Analysis of Variables and Descriptions of Islamic Finance Global Hub Index

Table 6.11: Islamic Finance Regulation and Supervision

A	Islamic Finance Regulation and Supervision	Mean	SD
1.	**Islamic Finance Court:** The establishment of Islamic finance court is important in the Islamic finance system to function as judgment for the Islamic finance disputes.	4.075758	0.75640
2.	**Islamic Finance Acts:** A sound, effective and robust acts' framework ensures the efficiency of the Islamic financial system.	4.41791	0.60676
3.	**Islamic Finance Guidelines:** The issuance of Islamic finance guidelines eases the function of the system.	4.373134	0.59888
4.	***Sharī'ah* Standards in Islamic finance:** Establishing *Sharī'ah* standards in Islamic finance is important to streamline various *Sharī'ah* interpretations and rulings in Islamic finance.	4.41791	0.60676
5.	**Islamic Finance Supervision and Audit:** The implementation of Islamic finance supervision and audit will fix and replace shortages in the right system.	4.253731	0.76561
B.	**Islamic Finance Talents: To evaluate Human Resources Sufficiency in a country, the following indicators are proposed to be included:**		
1.	**Number of Higher Education with Islamic Finance:**	4.164179	0.68749

	These are universities and colleges providing certificate or degree in *Sharīʼah* and Islamic Finance.		
2.	***Sharīʼah* Scholar:** *Sharīʼah* scholars are experts in *Sharīʼah* knowledge and other related fields of Islamic finance and provide consultation for Islamic finance institutions locally and globally.	4.238806	0.62980
3.	**Number of Training Centers in Islamic Finance:** The number of training centers that provides education and training in Islamic finance.	4.104478	0.67721
C.	**Islamic Finance Shares and Quantities**		
1.	**Islamic Finance Assets:** Volume of Islamic finance Shares in a country indicates the strength of Islamic finance institutions in terms of demand, size and performance.	3.8656716	0.67185
D.	**Islamic Finance Sectors: Aims to evaluate the performance of Islamic Finance Institutions in a country**		
1.	**Islamic Banks:** The number of Islamic Banks operating inside the country.	3.893939	0.82613
2.	**Islamic Insurance (Takaful):** The number of Islamic Insurance (Takaful) operating inside the country	3.878788	0.85094
3.	**Islamic Capital Market:** The number of Islamic Finance Capital Market products	3.848485	0.84561
E.	**Taxation: Aims to evaluate tax charges in a country**		
1.	**Corporate Tax, Personal Tax, Government Tax and Other Related Taxes:** Transparency, clarity, simplicity and predictability of financial reports are vital characteristics to be observed regarding to the taxation.	4.2089552	0.64049
F.	**Environment Support: Aims to Evaluate Supportive Element of Business Environment**		
1.	**Quality of Life:** Standard and quality of living promotes pleasant working environment and peace of mind.	4.268657	0.61748
2.	**Culture and Language:** Multilingual and healthy cultures of populations are among important factors of a country's Internationalization policy.	4.059701	0.73610
3.	**A Fair and Just Business Environment:** A fair and just business environment will ensure sound competition, fair legal decision and give the right to the entitled parties.	4.268657	0.61748
4.	**Infrastructure Support:** The availability of infrastructure support such ICT speed and security, reliable electricity and water supply, good highway networks and connections and other related infrastructure.	4.298507	0.57774
5.	**Government Responsiveness:** The government plays an important role in developing sound domestic business through the effective regulation, fair tax incentive and immediate response towards claims and corrections.	4.38806	0.57617
G.	**Cost: Aims to Evaluate the Cost Factor for Business Decision**		
1.	**Operational Costs:**	4.014925	0.66270

	The operational cost is important to be included in the assessment as this will determine the capability of the Islamic financial institutions to operate within the appropriate cost.		
2.	**Availability of Commercial Properties:** The availability of commercial properties in the country will promote the presence of foreign Islamic financial institutions to open the business inside the country.	3.835821	0.68749
H.	**Access: Aims to Evaluate the Availability of Access to the Customers and Services**		
1.	**Access to customers:** Access to customers means physical proximity to clients.	3.761194	1.00136
2.	**Access to international financial markets:** Refers to the IFI's networking with international players to facilitate cross border transaction.	4.089552	0.62113
3.	**Access to Suppliers of professional services:** Observing the availability of professional services such IT specialist, Expert Accountants both personal and firms, Legal Firms.	4.149254	0.58397
I.	**Liberalization Policy: Aims to Observe the Government Policy for Islamic Financial liberalization.**		
1.	**Government Liberalization Policy:** The government liberalizes the financial sector and approved licensed for foreign IFIs to operate in domestic market.	3.835821	0.64190
2.	**Number of Foreign Islamic Finance Institution Operating in the Country:** Observing the number of foreign IFIs operate inside the country.	3.850746	0.67988
3.	**Number of Local Islamic finance Institution Operates in Overseas:** Observing the number of local IFIs expand the business outside the country.	3.80597	0.74343
J.	**Category: Aims to Categorize Islamic Finance Service Country into National, Regional, International and Global Hub**		
1.	**National** A country that conducts Islamic financial services at the national level. The Islamic financial institutions operate inside the country and there is no license issued for foreign Islamic financial Institutions to operate inside the country.	3.656716	0.97782
2.	**Regional** A country that provides Islamic financial services within the national and regional areas. Local Islamic financial Institutions expand businesses inside the region and there are also licenses issued for the foreign Islamic financial institutions to operate.	3.865672	0.73640
3.	**International** A country that has a comprehensive system of Islamic finance consists of Islamic banks, Takaful and Islamic capital market. Local IFIs operates internationally. The country also issues license for International Islamic financial centres to operate inside the country.	3.940299	0.69371
4.	**Global Hub** The most integrated places for Islamic financial services institutions to directly connect national, regional and international financial services participants. Consist of full sector of Islamic Finance, namely Islamic Banks, Takaful and	3.939394	0.80366

	Islamic Financial Market. Number of foreign IFIs operates inside the country and local IFIs expand business globally.		

6.5 ANALYSIS AND RESULTS

6.5.1 Islamic Finance Regulation and Supervision

The survey questionnaire includes five items under the variable of Islamic finance regulation and supervision. In sum, all items under this variable scored more than 4 (out of total 5), which indicate the most accurate item for each subject. Item and description number two, "Islamic Finance Act: A sound, effective and robust acts' framework ensures the efficiency of the Islamic financial system," and number four, "*Sharī'ah* Standards in Islamic finance: Establishing *Sharī'ah* standards in Islamic finance is important to streamline various *Sharī'ah* interpretations and rulings in Islamic finance," shares the highest response among other subjects under this variable with the mean of 4.41791, which indicates the compulsory requirement to include the Islamic Finance act and *Sharī'ah* in the index. The establishment of the act is important to govern the system. Item and description number three, "Islamic Finance Guidelines: The issuance of Islamic finance guidelines eases the function of the system," scores 4.373134, which indicates the importance of supportive guidelines to be incorporated in the index. Item and description number five, "Islamic Finance Supervision and audit: The implementation of Islamic finance supervision and audit will fix and replace shortages in the right system," scored 4.253731, which indicates the requirement of supervision factor in Islamic finance index to enhance the regulation with a monitoring and observation system.

The first item and description, "Islamic Finance Court: The establishment of Islamic finance court is important in Islamic finance system to function as judgment for the Islamic finance disputes," scored 4.075758. This item scored the lowest compared to other items, which indicates the less important feature to be included under the variable of Islamic finance regulation and supervision.

Based on the above results, it is understood that the regulation and supervision factors are critical to be included in the Islamic finance global hub framework. However, the issue arises on the establishment of the Islamic finance court. As discussed in chapter five, three respondents out of four disagreed on the establishment of the Islamic finance court as in their opinion the requirement does not reach into that level and it is adequate to be handled in a civil court. This is due to the dispute that Islamic finance is claiming more from the bank against the clients. In addition, the number of cases is not greater than ordinary reported cases, which will not lead to the establishment of the Islamic finance court.

Perhaps, the modification is needed in this variable by taking out the item of Islamic finance court of which most Islamic finance countries do not have such a facility. However, other items should remain in the index as a measurement tool to verify the factor of Islamic finance regulation and supervision.

6.5.2 Islamic Finance Talents: Aims to Evaluate Human Resources Sufficiency in a Country.

Under this variable, item and description number two, "*Sharīʼah* Scholar: *Sharīʼah* scholars are experts in *Sharīʼah* knowledge and other related fields of Islamic finance and provide consultation for Islamic finance institutions locally and globally," receives the highest score of 4.238806, which indicates the importance of the presence of *Sharīʼah* scholars. Hence, the description of this item is considered as most accurate.

The second item and description, "Number of Higher Education with Islamic Finance: These are universities and colleges providing certificate or degree in *Sharīʼah* and Islamic Finance," scored 4.164179, which indicates that the vital factor of human talent development is through the establishment of universities and colleges that provide Islamic banking and finance courses.

The item and description number three, “Number of Training Centers in Islamic Finance: Number of training centers that provide education and training in Islamic finance,” scored 4.104478, which indicates the equal importance to subject number two as a supportive factor to produce skilled talents among Islamic banking and finance personnel.

Several series of interviews were conducted among Islamic finance scholars to seek their opinion pertaining to this issue as mentioned in chapter five. It could be concluded that all respondents agreed on the high demand for Islamic finance talents in all categories, especially in the high level of Islamic finance expert. Hence, the variable of “Islamic Finance Talents,” could be considered as among the most important element in the index. With the high score measurement result of the survey, hence, this variable will remain in the index without any modification.

6.5.3 Islamic Finance Shares and Quantities

This variable scored close to four. The item and description number one, “Islamic Finance Assets: Volume of Islamic finance shares in a country indicates the strength of Islamic finance institutions in terms of demand, size and performance,” scored 3.8656716. Perhaps, most of the respondents viewed size and shares as not a vital factor that contributes to the performance of Islamic banking and finance more than the availability of facilities. In fact, Islamic finance shares in some Islamic countries are bigger than other countries, but the availability of facilities in the country is less efficient compared to the lower shares countries.

Based on an interview with R7, the respondent viewed the asset factor in the index is not as important as the availability of facilities. According to R7, “Asset” factor is basically less important compared to the availability of infrastructure factor. Hence, the methodology in ranking a global hub country is meaningless without taking into account the availability of infrastructure as a prime consideration.

R7 responded:

> *"....for me the size of the asset (shares) is secondary,…whether you are first ranking or second ranking…but you have the world class infrastructure, you have the world class services, you have the world class facilities then you are qualified to become …Islamic finance global hub…."*

From the above study, it could be concluded that this variable is not resilient to be included in the index. Hence, as the result shows that this variable is less meaningful. Further amendments on this factor will be made in the new framework of Islamic finance global hub index.

6.5.4 Islamic Finance Sectors: Aims to Evaluate the Performance of Islamic Finance Institutions in a Country

The overall score of each item under this variable is less than four, which indicates the need to review the Islamic banking and finance sector. The other sectors of Islamic finance are Islamic money market, Islamic Equity market and many more. Perhaps, the inclusion of Islamic finance sector must include all sectors and not just in one sector such as Islamic capital market alone.

The first item and description, "Islamic Banks: The number of Islamic Banks operating inside the country," scored 3.893939. The second item is "Islamic Insurance (*Takaful*): The number of Islamic Insurance (*Takaful*) operating inside the country," scored 3.878788 and the third subject is "Islamic Capital Market: The number of Islamic Finance Capital Market products," with a score of 3.848485.

With regard to the sector that Islamic finance global hub's main criteria for the fulfillment, R6 viewed the necessity for a country to have a holistic system of Islamic finance, namely Islamic Banking, Takaful and Islamic Financial market, which consists of Islamic capital, Islamic money market, derivative and other Islamic financial market instruments. R6 agreed in categorizing Islamic finance sectors into Islamic banking and Takaful but disagreed in the limitation of Islamic capital market, which from his point of view should comprise the entire contracts of Islamic financial market such as Islamic money market, Islamic equity funds and others.

R6 responded:

> *"…. I agree in a broad category it is three but it could be deeper, you have to talk about stock market for example, …..derivatives, venture capital, private equity, funds, and so on so forth...."*

In responding to the same question, R7, however, agreed in the categorizing of Islamic finance sector into three categories as a main and ordinary classification. However, R7 viewed that it is unnecessary to have a whole system in a country and it is adequate to have the niche area or specialization area to indicate that the country is an expert in Islamic banking and finance. For example, Malaysia is well known as a country, which specializes in Islamic capital market and other countries with another specialization such as Takaful. R7 said:

> *"Let say I am the global hub, I am good in banking, Takaful and Islamic Capital Market ..in three component…..I might be global hub in….like Malaysia currently for instance we are very much advance in capital market, … our framework in sum in capital market, we are among the top for example, ok, so let say Malaysia become global hub in capital market, middle east become global hub in Takaful for instance……,*

Based on R7's view, it could be concluded that the result of Islamic finance Global Hub country will not just only one country to champion the title, but many countries can also champion the title with various specializations.

However, global hub, as mentioned earlier is a center for all banking and financing activities executed in one place. It is difficult to determine an Islamic finance global hub without the fulfillment of the entire system of Islamic banking and finance. The niche area is a second level, which arrives subsequently after the fulfillment of the entire system of Islamic banking and finance sector. Hence, R6's view is more acceptable and the modification of the Islamic banking and finance sector should comprise Islamic banking, Takaful and Islamic Financial Market.

6.5.5 Taxation: Aims to Evaluate Tax Charges in the Country

The item and description of this variable is "Transparency, clarity, simplicity and predictability of financial reports are vital characteristics to be observed regarding to the taxation," scored 4.2089552. This score indicates the significance of sound tax application towards IFIs.

This variable scored greater than four, which means the importance of this variable that it should remain in the index. From the interview data, there are no comments by the interviewees regarding this variable. Hence, this resulted in maintaining this variable in the index.

6.5.6 Environment Support: Aims to Evaluate Supportive Element of Business Environment

There are four items included under the environment support variable, which are quality of life, culture and language, a fair and just environment, infrastructure support and the government responsiveness. Impressively, all items received the scores of more than four, which obviously indicate the importance and vital factor to be included in the framework.

Item number one, "Quality of Life: Standard and quality of living promotes pleasant working environment and peace of mind," scored 4.268657. Item number two, "Culture and Language: Multi lingual and healthy cultures of populations are among important factors of a country's Internationalization policy," received the score of 4.059701. Item number three, "A Fair and Just Business Environment: A fair and just business environment will ensure sound competition, fair legal decision and give the right to the entitled parties," scored 4.268657. Item number four, "Infrastructure Support: The availability of infrastructure support such ICT speed and security, reliable electricity and water supply, good highway networks and connections and other related infrastructure," received the score of 4.298507 and the last item, "Government Responsiveness: The government plays important role in developing sound domestic business through the effective regulation, fair tax incentive and fast responsive towards claims and corrections," scored 4.38806.

With regard to the issue of infrastructure, R6 and R7 stressed the importance of the availability of infrastructure as a vital factor among others to establish the Islamic finance global hub country.

R6 stressed:

> *"I think the point number one is the resilient of the infrastructure. Meaning that if you don't really have a very robust and resilience and strong of infrastructure banking, so whatever you claim basically it doesn't make sense. Even you have different sectors like Takaful, like banking sector or capital market, but if you do not have supporting infrastructure that help you, so basically I don't think it is relevant to claim yourself as a hub."*

R6 added that non-Muslim country with an advanced infrastructure comprises of the updated Information Technology, the accuracy and the efficiency of services, the fast development of infrastructure and others will be ahead other Islamic finance countries and win the Islamic finance global hub race. Although, the ruling and resolution of Islamic instruments are made in Islamic countries, the implementation may be in other non-Muslim countries that have adequate infrastructure to apply the Islamic finance instruments. The main issue is not only a theoretical approval, but also the applicability of the system, which plays a vital factor to entitle a country as an Islamic finance global hub center.

R6 responses:

> *"In other non-Muslim country, for example like UK, Hong Kong and Singapore, they have a niche, then they may a big, one they are hub, because they have the infrastructure. They have the infrastructure because for this reason you just imagine,…in the case of Tawarruq, or Commodity Murabahah, …one it has been initiated the standard*

on the permissibility of debt…. it was…..in OIC resolution in mecca, but the practice of the Tawarruq started in UK."

Based on this study, it could be summarized that the availability of infrastructure is vital to become as a main variable in the index due to its high score and the proposal by both interviewees who agreed on the importance of the infrastructure factor. Hence, further amendments will be made on the framework to highlight infrastructure factor as the main variable in the index.

6.5.7 Cost: Aims to Evaluate the Cost Factor for Business Decision

Two items being included under this variable, namely the operational costs and the availability of commercial properties. Item number one, "Operational Costs: The operational cost is important to be included in the assessment as this will determine the capability of the Islamic financial institutions to operate within the appropriate cost," scored 4.014925, which indicates that the cost is among the main factors considered by many parties to make any decision pertaining to their business model or operational model. However, the second item, "Availability of Commercial Properties: The availability of commercial properties in the country will promote the presence of foreign Islamic financial institutions to open the business inside the country," scored lower than four (3.835821), which indicates that it is the less important factor to be included in the framework. Perhaps, it is understood that the global financial centre might not be facing this problem since the availability of commercial properties is a primary and basic infrastructure to be facilitated from the beginning.

In responding to the question on the cost, R6 viewed that the cost factor is less important and perhaps inconsistent to other variables due to the understanding of the meaning of cost. To some extent, cost is meaningless when it comes to a huge financial funding on the development of many sectors like human capital development sector, infrastructure sector and other related sectors in Islamic banking and finance. This is due to the world-class infrastructure, which means a lot of monies were invested for the world-class level. The establishment of a number of Islamic finance institutions involved a huge fund as well. Hence, R6 viewed the difficulty to determine the cost factor that influences the establishment of an Islamic finance global hub center.

R6 said:

> *"…cost ..yes cost is equal important in competition, but cost some time you see, no doubt it is important but sometime it is difficult to control it. You know why, because …they call ……cost is a… we are not talking about the cost of the operation….I am talking about the cost of the whole business model…the cost of talent for example…the cost of living …If you are living in Singapore….which is not like in Malaysia…or you have someone …sometimes you cannot control because this is a standard of the country. Mmm…sometime we need professional talent, so you pay more….in your business ….I agree it is important element, to run to sustain the business….this is standard operation…sometimes it is difficult to monitor it because this is out of our control."*

However, R7 viewed that the cost factor plays a vital role in business decision. According to R7, cost is a factor that influences certain parties to conclude business decisions. Hence, cost should not to be ignored in the variable due to some parties' consideration.

R7 stressed:

> *"From the cost factor…I mean that is very important….. it is a competitive world …if people want to do something in Islamic finance, they look to Malaysia and they make a comparison for instance Dubai, …. Let say the cost of operation in dubai is cheaper …. So…why must they come here (to Malaysia)……that is one of the primary concern we say ….cost is one of the primary concern….sometime…some person….let say…they would able to compromise other things, but when it comes to cost, they want to be the most competitive…"*

Based on the above study, a result merely suggests maintaining the cost factor in the variable based on the measurement using the Likert Scale, which shows a significant number greater than two. This measurement is supported by R7's view. Hence, the cost factor will be maintained in the framework.

6.5.8 Access: Aims to Evaluate the Availability of Access to the Customers and Services

Access variable is important to ensure the smooth running of business without any access obstacle. Under this variable, item number three, "Access to suppliers of professional services: Observing the availability of professional services such IT specialist, Expert Accountants both personal and firms, Legal Firms," received the highest score of 4.149254, which indicates the importance of industry to get the service from the expert and professionals. Item number two, "Access to international financial markets: Refers to the IFI's networking with international players to facilitate cross border transaction," scored 4.089552. However, item number one, "Access to customers: Access to customers means physical proximity to clients," scored the lowest compared to other item with a score of 3.761194.

Two out of three items under "Access" variable scored greater than four while the rest score closer to four. From this result, it is important to note that "access" is a vital factor to be included in the index. There are no comments from the interviewees regarding this variable and items, and hence, indicates the reliability of "Access" to be maintained in the index.

6.5.9 Liberalization Policy: Aims to Observe the Government Policy for Islamic Financial Liberalization.

All items under this variable scored under four points and each of the point is closer to one another. Perhaps, this topic is not a familiar topic to the respondents. In fact, the liberalization policy is one of important tools for the establishment of a global hub country. Item number one, “Government Liberalization Policy: The government liberalizes the financial sector and approved licensed for foreign IFIs to operate in domestic market,” scored 3.835821. Second item, “Number of Foreign Islamic finance Institution Operates in country: Observing the number of foreign IFIs operate inside the country,” received a score of 3.850746 while item number three, “Number of Local Islamic finance Institution Operates in Overseas: Observing the number of local IFIs expand the business outside the country,” scored 3.80597.

With regard to the score result, as mentioned in the beginning, perhaps the word “liberalization,” portrays a picture, which is not in alignment with the original intention by the researcher.

The aim from the using of word “liberalization” is to connote the opening of local market to foreign players. There are certain controls and limitations by the Central Bank of Malaysia as mentioned by R1 and not a common understanding of liberalization in the global practice. However, some respondents understood the intention of this variable, and thus, contributes to the high score result to become closer to four.

Based on the interview results, there is no comment pertaining to this variable by the scholars. Perhaps, the scholars noted this variable and understood the global hub idea is derived from the financial liberalization policy.

6.5.10 Category: Aims to Categorize Islamic Finance Service Country into National, Regional, International and Global Hub

Categorizing countries into four categories namely national, regional, international and global hub might raise a question to respondents, which influences the score points. Overall items scored under four points. Item number one, “National**:** A country which conducts Islamic finance services within National level. The Islamic financial institutions operate inside the country and there is no license issued for foreign Islamic financial Institutions to operate inside the country," scored 3.656716. Item number two, "Regional: A country which provides Islamic finance services within the national and regional areas. Local Islamic financial Institutions expand businesses inside the region and there are also licenses issued for the foreign Islamic financial Institutions to operate," received a score of 3.865672. Item number two, "International: A country which having a comprehensive system of Islamic finance consist of Islamic banks, Takaful and Islamic capital market. Local IFIs operates internationally. The country also issues a license for International Islamic financial centers to operate inside the country," scored 3.940299 and the last item, "Global Hub: The most integrated places for Islamic financial services institutions to connect national, regional and international financial services participants directly. Consist of full sector of Islamic Finance namely Islamic Banks, Takaful and Islamic Financial Market. Number of foreign IFIs operates inside the country and local IFIs expand business globally," scored 3.939394.

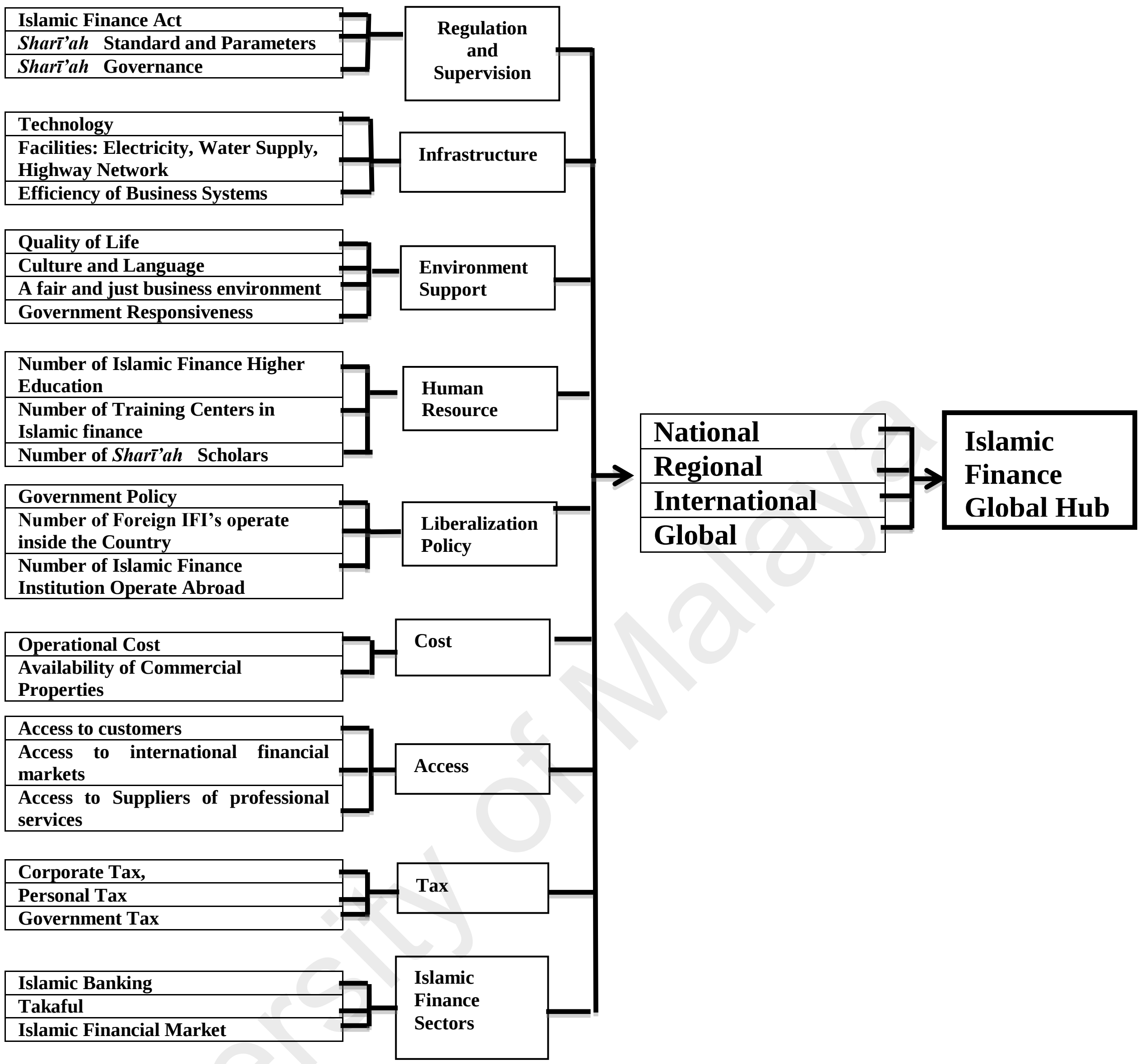
Although the score of each item is less than four, most of the scores are very close to four. Perhaps some respondents could not capture the prime objective of diversifying the Islamic finance country into four categories. Categorizing Islamic finance countries into four categories are important to include all countries in the index.

There are no comments from Islamic finance scholars pertaining to the index, which could be concluded as the consent of the scholars on the availability of this variable.

6.6 A Proposal for an Islamic Finance Global Hub Framework

Based on the above study, a conclusion has been made to finalize the framework with some amendments as measured in the scale and the interview analysis. Hence, the new framework of Islamic finance global hub index is proposed as follows:

Diagram 6.2: Proposal for the Islamic Finance Global Hub Framework



6.7 PROPOSAL FOR A NEW DESCRIPTION OF ISLAMIC FINANCE GLOBAL HUB INDEX

Table 6.12: Description of Each Assessment Subjects

	Subject and Description	
	Regulation and Supervision	
1.	Islamic Finance Acts	A sound, effective and robust acts' framework ensures the efficiency of the Islamic financial system.
2.	*Sharī'ah* Standards and Parameters	Establishing *Sharī'ah* standards in Islamic finance is important to streamline various *Sharī'ah* interpretations and rulings in Islamic finance.
3.	*Sharī'ah* Governance	The implementation of Islamic finance supervision and audit will fix and replace shortages in the right system.
	Infrastructure	
1.	Technology	The availability of advanced technology in ICT and

		advanced new technological products in various areas, especially in the financial system.
2.	Facilities: Electricity, Water Supply, Highway Network and Transportation	The availability of facilities in a country such as electricity, water supply, highway network and transportation.
3.	Efficiency of Business Systems	The efficiency of business system consists of the accuracy of time factor, fast approval, less of bureaucracy, fast arrangement, competency and productivity.
	Environment Support	
1.	Quality of Life	Standard and quality of living promotes pleasant working environment and peace of mind.
2.	Culture and Language	Multilingual and healthy cultures of populations are among important factors of a country's internationalization policy.
3.	A fair and just business environment	A fair and just business environment will ensure sound competition, fair legal decision and give the right to the entitled parties.
4.	Government Responsiveness	The government plays important role in developing sound domestic business through the effective regulation, fair tax incentive and fast response towards claims and corrections.
	Human Resource	
1.	Number of Islamic Finance Higher Education	These are universities and colleges providing certificate or degree in *Sharī'ah* and Islamic Finance.
2.	Number of Training Centers	Number of training centers that provide education and training in Islamic finance.
3.	Number of *Sharī'ah* Scholars	*Sharī'ah* scholars are experts in *Sharī'ah* knowledge and other related fields of Islamic finance and provide consultation for Islamic finance institutions locally and globally.
	Liberalization Policy	
1.	Government Policy	The government liberalizes the financial sector and approved licensed for foreign IFIs to operate in domestic market.
2.	Number of Foreign IFI's operate inside the Country	Observing the number of foreign IFIs operating inside the country.
3.	Number of Islamic Finance Institution Operate Abroad	Observing the number of local IFIs that expand the business outside the country.
	Cost	
1.	Operational Costs	The operational cost is important to be included in the assessment as this will determine the capability of the Islamic financial institutions to operate within the appropriate cost.
2.	Availability of Commercial Properties	The availability of commercial properties in the country will promote the presence of foreign Islamic financial institutions to open the business inside the country.
	Access	
1.	Access to customers	Access to customers means physical proximity to clients.
2.	Access to International Financial Markets	Refers to the IFI's networking with international players to facilitate cross border transaction.
3.	Access to Suppliers of	Observing the availability of professional services

	Professional Services	such IT specialist, Expert Accountants both personal and firms, Legal Firms.
	Tax	
1.	Corporate Tax, Personal Tax, Government Tax	Transparency, clarity, simplicity and predictability of financial reports are vital characteristics to be observed regarding to the taxation.
	Islamic Finance Sectors	
1.	Islamic Banking	The number of Islamic Banks operating inside the country.
2.	Takaful	The number of Islamic Insurance (Takaful) operating inside the country
3.	Islamic Financial Market	*The availability of Islamic Financial Market in a country such as Islamic capital market, Islamic money market and others indicate the completion of the Islamic finance system.
	Categories	
1.	National	A country, which conducts Islamic financial services within National level. The Islamic financial institutions operate inside the country and there is no license issued to foreign Islamic financial Institutions to operate inside the country.
2.	Regional	A country, which provides Islamic financial services within the national and regional areas. Local Islamic financial Institutions expand businesses inside the region and there are also licenses issued for the foreign Islamic financial Institutions to operate
3.	International	A country which having a comprehensive system of Islamic finance consist of Islamic banks, Takaful and Islamic capital market. Local IFIs operates internationally. The country also issues license for International Islamic financial centres to operate inside the country.
4.	Global	The most integrated places for Islamic financial services institutions to connect national, regional and international financial services participants directly. Consist of full sector of Islamic Finance namely Islamic Banks, Takaful and Islamic Financial Market. Number of foreign IFIs operates inside the country and local IFIs expand business globally.

6.8 CHAPTER SUMMARY

In the recent years, Islamic banking and finance has successfully emerged as an alternative to the conventional financial system. Many countries around the world have made amendments to their law to permit the establishment of Islamic finance system. Up to date, there are fifty countries around the world that provide Islamic banking and finance services. A constant development of Islamic banking and finance and the expansion of the service due to the introduction of new products have integrated the system to become available as a comprehensive financial system to stay in parallel with the conventional financial system.

Some advanced Islamic finance countries announced their strategic plans to become Islamic finance global hub centers. Many countries including the advanced economic countries such as London, Singapore and Hong Kong and the well-known Islamic finance countries such as Malaysia and U.A.E have put a clear path and vision to become an Islamic finance global hub as their prime objective. Hence, an exact measurement is needed to ascertain the requirement for the Islamic finance global hub status. It is obvious that certain criteria need to be fulfilled before any claims can be made. The criteria such as the availability of infrastructure, the robust regulation of Islamic finance, the advanced system of technology and other related criteria are among the vital factors, which are important in the measurement.

This study brings three assessment bodies with the objective to evaluate the available factors to be included in the new framework of Islamic finance global hub index. The selection of the factor, were made from all assessment bodies and the most relative factor will be adopted from each assessment body to be applied in the new proposal of Islamic finance global hub index. As such, this framework requires approval and verification from expert to ensure the index is viable. Two methods were applied in order to verify the framework, namely the interview and the survey method. As a result, a new framework of Islamic finance global hub index is proposed in this study after certain amendments and corrections were made based on the previous analysis.

7.0 CONCLUSION AND PROPOSALS

7.1 CONCLUSION

Islamic finance in Malaysia has illustrated a significant rapid development since its commencement in 1983 until present. The Central Bank of Malaysia as the regulator in the Malaysia financial system plays a vital role in confirming a sustainable Islamic finance system in Malaysia and ensures the Islamic financial system is as competent as its conventional counterpart. There were immense efforts and time allocated to certify the sound, robust and resilient Islamic finance system. Due to the fact that the Islamic finance system is supported by a strong recovery package, which is important in functioning as risk management tools, most of the countries around the world started to look after this alternative financial and economic system as a remedy for the present economic and financial problems.

The study conducted in the second chapter was on the Malaysian Islamic finance system, which comprises of Islamic banking, *Takaful* and Islamic financial market. This study found that Malaysia had successfully developed an integrated Islamic finance system in the country. This successful effort is steered by the following key formulas:

1. An effective role played by the regulators namely the Central Bank of Malaysia and the Securities Commission had successfully formed a comprehensive system of Islamic finance consists of the Islamic banking system, *Takaful* and Islamic financial market.
2. The Malaysian government provides a strong support for the success of Islamic finance, especially in approving the regulations to fit Islamic finance requirement and involves effectively in promoting Malaysia as an Islamic Finance Global Hub through tax reduction and other measures.
3. Compared to other Islamic finance countries, among the specialty of Malaysia is on product development and innovation. This has integrated the Islamic financial

system and able to serve the clients in various sectors of Islamic financial instruments.

4. A big number of Islamic financial institutions provide effective and quality services.

5. Excellent framework of *Sharī'ah* management, which comprises of the *Sharī'ah* advisory council of the Central Bank of Malaysia and the Securities Commission, the *Sharī'ah* committee of Islamic finance institutions and supported by the *Sharī'ah* units in each Islamic finance institution, provides a well *Sharī'ah* consultation and proper issuance of *Sharī'ah* rulings and deliberation.

6. Continued research and studies intensified by various parties from the regulators, Islamic financial institutions, higher learning institutions and the government.

The Islamic financial system development around the world has reached its completion, which remarks the development of a thorough financial system comprises of the Islamic banking, *Takaful* and Islamic capital market. In the past, a "basic" traditional financial system typically comprised simple currency, simple payment, simple banking and simple insurance activities. David Reim and Charles Calomiris suggested that:

"The most primitive function of a financial system is to issue and safeguard money. The next function to evolve is a payment mechanism, typically a check-clearance system, which enables parties to transfer money among each other without taking the risk of delivering it in coin or currency. These basic functions are the domain of banks, which are invariably the first financial institutions to evolve in a developing country."

A "developed" financial system provides effective allocations of resources via market pricing as well as a variety of instruments and risk management functions.

Furthermore, the idea of Islamic finance hub came out through all Islamic finance countries' future plans, which is a sign of a pleasant development of Islamic finance. Many countries such as Malaysia, Bahrain, Qatar, Pakistan and even other countries or financial centres such as London, Hong Kong and Singapore set the Islamic finance global hub objective as their supreme vision.

Chapter three focuses on the philosophy of global hub, which has a historical evaluation that began with the expansion of banking and finance business. The process continues to position the country as a financial global hub area and as an attraction place for worldwide business entities. This chapter elaborates significantly the meaning of globalization as well as the process of how the global hub began. At the end of this chapter, the meaning of Islamic finance global hub is defined. This definition, currently, does not exist in nature, but based on the previous and robust study conducted in this chapter.

Chapter four discovers the role of the Central Bank of Malaysia in positioning Malaysia as a global hub country. Among the measures taken by the Central Bank of Malaysia are; strengthening the regulatory policy and supporting frameworks, the establishment of the financial sector master plan (FSMP), the establishment of the Malaysia International Islamic Financial Centre (MIFC), strengthening *Sharī'ah* factors and developing the centre for human capital development in Islamic Finance.

This study concludes that Islamic finance sector in Malaysia has been seen as the most progressive and attractive for investment with the offering of various incentives plans and further liberation in the coming years. Furthermore, the achievement of Malaysia in Islamic finance comprises the entire sectors such as in market institutions and Islamic financial products, in capital flows, and in strategic planning to establish the country as a dominant position in the world of Islamic finance. Malaysia has also become the leading player in the global Sukuk (Islamic bond) market and in developing innovative products in money markets, derivatives, and in liquidity management.

The strong and comprehensive regulatory and supervisory framework is among the strengths of Malaysia's Islamic finance system. This includes a stronger standard of corporate governance, disclosure, accountability, transparency, market discipline, risk management and customer protection. The key stimulating elements that drive the development of Islamic finance in Malaysia could be highlighted as follows:[500]

8. Stability: Malaysia has enjoyed political, social and economic stability with a consistent stability over the last 50 years, which condition enables the environment to grow.

9. Government Support: Continuous support from the government of Malaysia with dedicated laws, tax neutrality and tax incentives.

10. Central Bank: The Central Bank of Malaysia has consistently driven the Islamic finance development with a comprehensive regulatory framework, institutional and infrastructure building and strong consumer education.

11. Approach of implementation: Gradual and incremental approach, for instance, the commencement of one Islamic bank followed by the permission for Islamic window license, the liberalization of Islamic banks and the Islamic subsidiaries.

12. Stakeholders: Strong buy-in by relevant stakeholders (e.g., other regulators, financial players, the *"rakyat"* Muslims and non-Muslims alike).

13. Branding: Branding of Islamic finance as a business consideration as opposed to religious consideration and selling value propositions.

[500] Ahmad Hizzad Baharuddin, "The Regulatory Framework of Islamic Financial System in Malaysia," (Director of Islamic Banking and Takaful Department of Bank Negara Malaysia's Presentation on 18 April 2011), 10.

14. Innovation: Strong advocator of innovation and brave ideas – both domestic & international – sukuk issuance, Ar Rahnu, IFSB, IILM.

Although Malaysia has done sufficient measures comprising several initiatives in enhancing Islamic finance in Malaysia, a critical study is imperative to examine some issues regarding the incomplete matter such as the issue of harmonization in *Sharī'ah* deliberation and fatwas, the effect of liberalization towards local market, the *Sharī'ah* product issues such as the BBA, which is still raising an issue among customers and others. Finally, it is worth to note that the study on the Central Bank of Malaysia 's initiatives in positioning Malaysia as a global hub for Islamic finance yields several findings as follows:

5. This study updates the recent policy taken by the Central Bank of Malaysia regarding the development of Islamic finance in Malaysia.

6. This study has found the existence of competition among countries in the world to become the leading country in Islamic banking and finance, which in fact benefits the system.

7. This study provides lucrative information regarding the measures taken by the Central Bank of Malaysia in positioning Malaysia as a global hub for Islamic finance.

8. Finally, this study has provided updated figures of Islamic banking and finance performance.

Chapter 5 analyses the interviews from the respondents of the Central Bank of Malaysia and the Islamic Financial Services Board, practitioners and *Sharī'ah* experts. The verification regarding to the Central Bank of Malaysia 's vision towards becoming as Islamic finance global hub presented in this chapter is valuable and vital to support this study. Simultaneously, Malaysia's policy in controlling the competition among foreign and local institutions also requires a clear view from the regulator. As a conclusion, the majority of respondents agreed that the government of Malaysia through the Central Bank of Malaysia visions the country to becoming as Islamic Finance Global Hub. This vision becomes as the Malaysian's government national agenda. In addition, the Central Bank of Malaysia has strategized a clear framework in their ten years Financial Sector Master Plan to position Malaysia as an Islamic finance global hub.

With regard to Malaysia's competitiveness, compared to other countries, most of the respondents agreed on the privilege of Malaysia in terms of the speciality in *Sharī'ah* related matters such as the advancement in Islamic finance products, sufficient talents in Islamic finance and supportive Islamic culture. Hence, Islamic finance in Malaysia caters for the whole segments of Islamic finance such as retail banking, project financing, *Takaful* coverage and Islamic capital market. Malaysia also enjoys the advancement of technologies and efficiency together with experts and trained officers available in the industry.

The global hub policy exposes the country into an open competition between foreign and local institutions. With regard to this issue, the Central Bank of Malaysia has set up a control policy where all foreign banks are allowed to open the subsidiaries. Through this policy, foreign banks are restricted from channelling their revenues into their own head quarter's country. However, the competition still exists between the foreign and local industries or among the local Islamic finance institutions themselves. Despites the negative impacts of competition, some respondents viewed that this competition will also bring positive impacts such as the improvement of management, the development of new products and the introduction of new technologies.

Most of the respondents agreed on the requirement for the establishment of a special assessment body in categorizing the Islamic finance global hub. This is due to many claims among Islamic finance countries as Islamic finance global hubs. A free and independent body of Islamic finance global hub index could support a fair and just assessment of the Islamic finance global hub.

Chapter six studies three assessment bodies, namely Ernst & Young, Global Competitiveness Report and the Global Financial Center Index. This study aimed at analysing the comparison between three assessment bodies. The methodology used in determining the country's economic performance was selected and adopted in the new framework to function in assessing Islamic finance global hub countries. In order to verify this framework, a mix-method analysis was applied, namely the interview method and the survey method. Each variable was analysed using the descriptive-mean method and Islamic finance experts' views. The combination of both methods is a just procedure to provide adequate verification on the framework.

Chapter 7 is the last chapter, which consists of the conclusion and the proposals.

7.2 PROPOSAL

7.2.1 The Meaning of Islamic Finance Global Hub

It is clearly understood that the financial global hub does not only involve finance, but also investment and trade. Thus, the interpretation of Islamic finance Global Hub is proposed as "A country becomes as a hub for local and global financial providers in offering Islamic finance services comprises of Islamic banking, *takaful* and Islamic financial market for country's residents and International customers."

However, in term of the pronunciation, some pronounce it as a "Global hub for Islamic Finance," while others refer to it as "Islamic Finance Global Hub." Regardless of the pronunciation, the meaning refers to the same understanding.

7.2.2 Proposal: A new Islamic Finance Global Hub Index

As presented in chapter 5, there are three organizations and companies being reviewed to determine the most accurate method in determining the financial centre, namely The Global Competitiveness Report, The Global Financial Center Index and the Ernst & Young (E&Y) Globalisation Index 2011. The study found that the most accurate methodology is as applied by the Global Financial Center Index (GFCI) and the Ernst & Young (E & Y) Globalization Index 2011.

The most important thing in this study is; how did the financial centres being categorized by the GFCI? The answer is by using the three elements of evaluation. The first element is 'connectivity', which is considered as an extent to which a centre is well known around the world and how much non-resident professionals believe it is connected to other financial centres.[501] A centre's connectivity is assessed using a combination of 'inbound' assessment locations (the number of locations from which a particular centre receives assessments) and 'outbound' assessment locations (the number of other centers assessed by the respondents from a particular centre). If the weighted assessments for a centre are provided by over 60% of other centres, this centre is deemed to be 'Global'. If the ratings are provided by over 45% of other centres, this centre is deemed to be 'transnational.' The second element is 'Diversity', which means the breadth of industry sectors that flourish in a financial centre. The GFCI considers this 'richness' of the business environment to be measurable in a similar way to that of the natural environment and therefore, use a combination of biodiversity indices (calculated on the instrumental factors) to assess a centre's diversity. A high score means that a centre is well diversified while a low diversity score reflects a less rich business environment. [502]

---

[501] *Ibid.*, 8.
[502] *Ibid*.

Hence, in the effort to develop an Islamic Financial centre index, the existence framework applied in the GFCI could be used as a benchmark. As discussed in Chapter 6, the main factors of Global financial centre assessment use the following criteria:

1. The availability of skilled personnel
2. The regulatory environment
3. Access to international financial markets
4. The Availability of business infrastructure.
5. Access to customers
6. A fair and just business environment
7. Government Responsiveness
8. The Corporate tax regime
9. Operational Costs
10. Access to Suppliers of professional services
11. Quality of Life
12. Culture and Language
13. Quality/ Availability of Commercial property
14. The personal tax regime

As to comply with the Islamic requirements, the Islamic factors are proposed to be included in the evaluation where it is drafted as follows:

7. A strong *Sharī'ah* supervision control to ensure all Islamic finance Institutions comply with *Sharī'ah*. For instance, the control on Islamic credit card usage, which is only applicable in Halal premises.
8. The establishment of the *Sharī'ah* court for the settlement of Islamic finance dispute, which is vital to ensure the case hearing in the best manner with

sufficient Islamic finance knowledge among the judges, the advocates and all the involved parties.

9. Sufficient number of *Sharī'ah* compliant products in Islamic banking, *Takaful* and Islamic capital market.
10. Good asset liquidity management to ensure Islamic finance funds do not leak into non-Halal business.
11. Strong Islamic finance application includes Islamic banking, Islamic Capital Market and Islamic Insurance.
12. Huge shares of Islamic finance in the economy provide well acceptance among people.

With the combination of both methods, the new Islamic financial centre index will determine the *Sharī'ah* compliance aspect, together with other technical features. Cities such as London, Hong Kong and Singapore are now offering Islamic finance facilities and have also claimed to be the global hubs for Islamic finance. However, the offering of Islamic finance services is not sufficient without a strong application in *Sharī'ah* aspects. Therefore, a new framework to evaluate the Islamic financial center was proposed in this study.

7.2.3 Proposal: Features for the Islamic Finance Global Hub Index

First and foremost the number of Islamic finance countries is vital to count as it will create a big player of Islamic finance providers and then, selection can be executed.

7.2.3.1 List of the Islamic Finance Countries

Table 7.1: Islamic Finance Countries

Continental	Num	Countries
Africa	1.	Republic of Nigeria
	2.	Republic of South Africa
	3.	Republic of Sudan
	4.	Arab Republic of Egypt

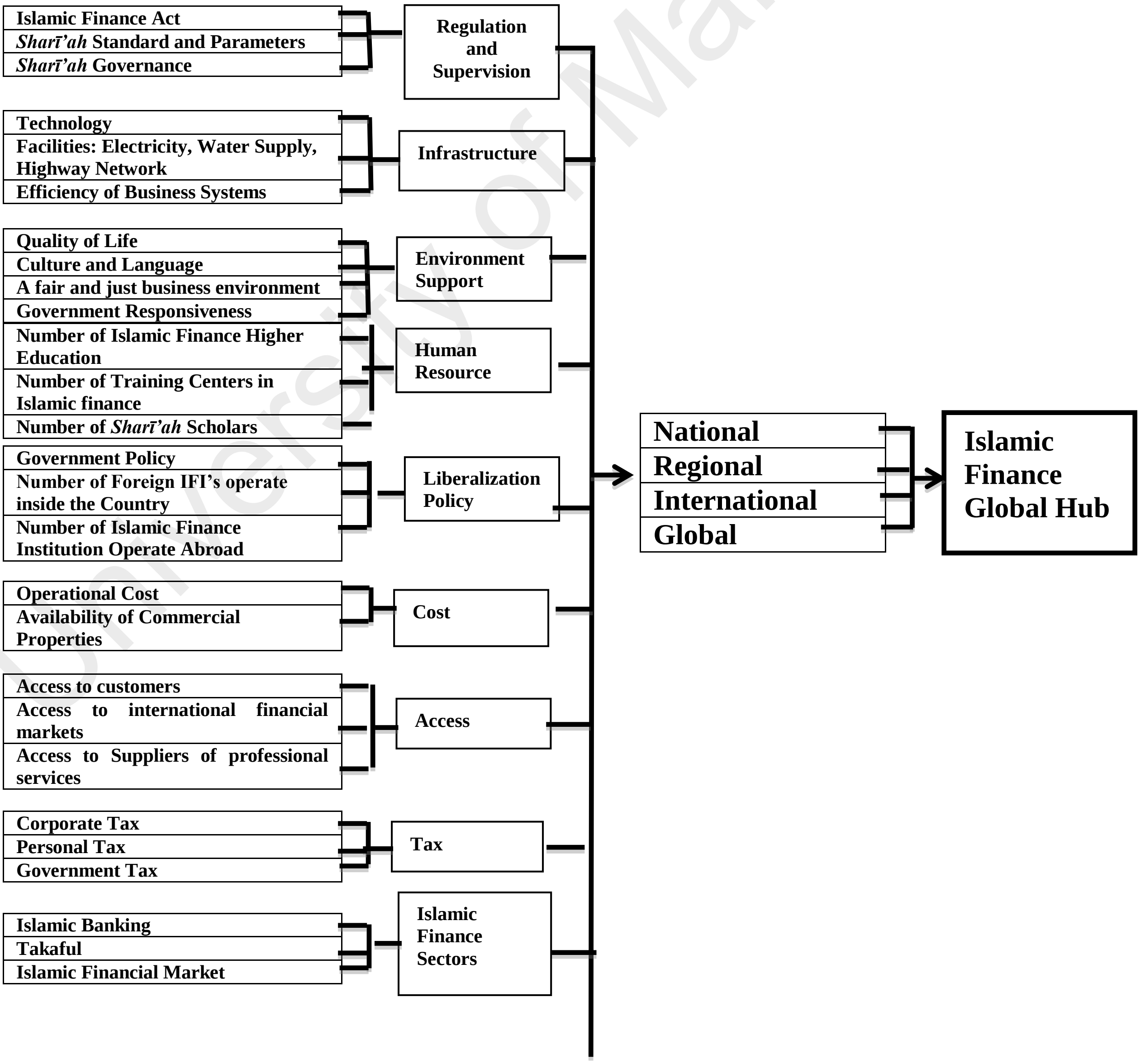
	5.	Republic of Ghana
	6.	Kingdom of Morocco
	7.	Republic of Kenya
	8.	Republic of Tunisia
	9.	Republic of Mauritius
	10.	Republic of Senegal
	11.	Islamic Republic of Mauritania
Asia	1.	Malaysia
	2.	Islamic Republic of Pakistan
	3.	Republic of Indonesia
	4.	Negara Brunei Darussalam
	5.	Republic of Singapore
	6.	Democratic Socialist Republic of Sri Lanka
	7.	Republic of Turkey
	8.	Islamic Republic of Afghanistan
	9.	Australia
	10.	Republic of Azerbaijan
	11.	People's Republic of Bangladesh
	12.	People's Republic of China
	13.	Hong Kong Special Administrative Region
	14.	Republic of India
	15.	Japan
	16.	Republic of Kazakhstan
	17.	Russian Federation
	18.	Republic of Korea
	19.	Kingdom of Thailand
Europe	1.	Republic of Ireland
	2.	Grand Duchy Luxembourg
	3.	United Kingdom of Great Britain and Northern Ireland
	4.	Republic of France
	5.	Federal Republic of Germany
	6.	Republic of Italy
	7.	Republic of Malta
Middle East	1.	Kingdom of Bahrain
	2.	State of Kuwait
	3.	State of Qatar
	4.	Kingdom of Saudi Arabia
	5.	United Arab Emirates
	6.	Hashemite Kingdom of Jordan
	7.	Islamic Republic of Iran
	8.	Republic of Iraq
	9.	Republic of Lebanon
	10.	Sultanate of Oman
	11.	Republic of Yemen
North America	1.	United State of America
	2.	Canada

Total Islamic Finance Countries: 50		

Source: Global Islamic Finance Forum 2012 (GIFF)

7.2.3.2 Islamic Finance Global Hub Framework

Diagram 7.1: Islamic Finance Global Hub Framework:



7.2.3.3 Description of Each Assessment Subject

Table 7.2: Description of Each Assessment Subject

Subject	Description
Shares and Quantities	
Islamic Finance Shares	To identify Islamic finance Shares in the country, which will indicate the strength of Islamic finance institutions in terms of demand, size and performance.
Number of foreign Islamic finance Institution Operate in the country	To observe the policy of the government in terms of liberalization policy to position the country as the world Islamic finance service provider.
Number of Islamic Finance Institution Operating Abroad	To identify the performance of local Islamic finance institutions in order to determine the efficiency, sustainability, competency and International standard services.
TAX	
Corporate Tax, Personal Tax, Government Tax and Other Related Taxes	Transparency, clarity, simplicity and predictability are vital to be observed regarding to the tax matter.
Environment Support	
Quality of Life	Standard and quality of living promote pleasant working environment and peace of mind.
Culture and Language	Multilingual and good cultures of populations are among important factor of a country's internationalization policy.
A fair and just business environment	A fair and just business environment will ensure sound competition, fair legal decision and give the right to the entitled parties.
Infrastructure Support	To determine the availability of infrastructure support such as ICT speed and security, Electricity and water supply, highway networks and connections and other related infrastructure.
Government Responsiveness	The government plays important role in developing sound domestic business through affective regulations, tax reduction and immediate response towards claims and corrections.
Cost	
Operational Costs	The operational cost is important to be included in the assessment as this will determine the capability of the Islamic financial institutions to operate within the appropriate cost.
Availability of Commercial Properties	The availability of commercial properties in the city country will promote the presence of foreign Islamic financial institutions to open the business inside the country.
Human Resources	
Number of Islamic	The existence of number of higher education/ learning

Finance Higher Education	will promote the issuance of many human capital sources and, hence, will provide the institutions a variety of options in choosing the most suitable staff.
Number of *Sharīʼah* Scholars	*Sharīʼah* scholars play a very important role in Islamic finance as they function to approve Islamic finance products and policies, to provide *Sharīʼah* opinions and to clarify any ambiguity in Islamic finance.
Regulation and Supervision	
Islamic Finance Court	The establishment of Islamic finance court is important in the Islamic finance system to function as arbitrator for Islamic finance disputes.
Islamic Finance Acts	Sound, affective and robust acts' framework will ensure the efficiency of the Islamic financial system.
Islamic Finance Guidelines	The issuance of Islamic finance guidelines will ease the function of the system.
***Sharīʼah* Standards in Islamic finance**	*Sharīʼah* standard in Islamic finance is important to streamline various *Sharīʼah* interpretations and rulings in Islamic finance.
Islamic Finance Supervision and audit	Islamic finance system is also exposed to abuse actions and wrongdoings from any person who will put the system incompliance with *Sharīʼah*. Thus, the supervision will ensure any mistake is fixed and replaced into the right order.
Access	
Access to customers	Access to customers means physical proximity to clients.
Access to international financial markets	Refers to the IFI's networking with international players to facilitate cross border transaction.
Access to Suppliers of professional services	To observe the availability of professional services such as the IT specialist, expert accountants both personal and firms, and legal Firms.

7.2.3.4 Description of the National, Regional, International and Global Hub of Islamic Financial Country

Table 7.3: Description of the National. Regional, International and Global Hub of Islamic Financial Country

National Islamic Financial Country	A country that conducts Islamic financial services at the national level. The Islamic financial institutions operate inside the country and there are no licences opened to the foreign Islamic financial Institutions to operate inside the country.
Regional Islamic financial Country	Defined as a country that provides Islamic financial services within the regional areas. Islamic financial institutions operate businesses within the region and there are also licences opened to the regional Islamic financial institutions.
International Islamic financial Country	Refers to a country where the Islamic financial institutions operate at the international level. The country also opens licences for foreign Islamic financial centres to operate inside the country. A large volume of cross-border transactions is conducted whereby these

	transactions include at least two locations in different jurisdictions.
Islamic Finance Global Hub Country	The most integrated places for Islamic financial services institutions to connect international, national and regional financial services participants directly.

7.2.4 Proposal to Enhance Human Capital Development

A proposal to resolve human capital shortage should consider some measures for Islamic finance authorities as follows:

7. Co-operation network between regulators, academic institutions and industry players to set up a proper framework to develop an Islamic Finance talent.
8. Incentives offerings to related Islamic Finance talents to sustain their services.
9. To increase fund for staff training.
10. To co-operate with other Islamic finance scholars from other countries in mutual knowledge and experience sharing.
11. Creating awareness of Islamic finance among the public.
12. In increasing domestic Islamic finance expert, a special treatment by the government could be considered for the foreign Islamic finance scholars such as allowing Malaysian permanent residence to serve in Malaysia for a long period.

As reported by INCEIF, out of 1710 students (2006-2010), only 27 students or less than 2% from *takaful* industry; all sponsored by only 1 *Takaful* Operator.[503]

7.2.5 More Shares for Islamic Finance in the Economy

[503] Global Takaful Group, "Critical issues Facing Takaful Operators With Special reference to Malaysia," retrieved on 16 October 2012, http://www.globaltakafulgroup.org/sites/default/files/Syed%20Moheeb .%20Critical%20Issues%2022%20Nov%202011.pdf.

Islamic finance shares in Malaysia are still low in percentage. In 2010, Islamic finance shares represent only for 29% from total economic shares.[504] The percentage is still low compared to other Islamic finance providers and this number becomes disputable for Malaysia's capability to become as the top global Islamic finance hub.

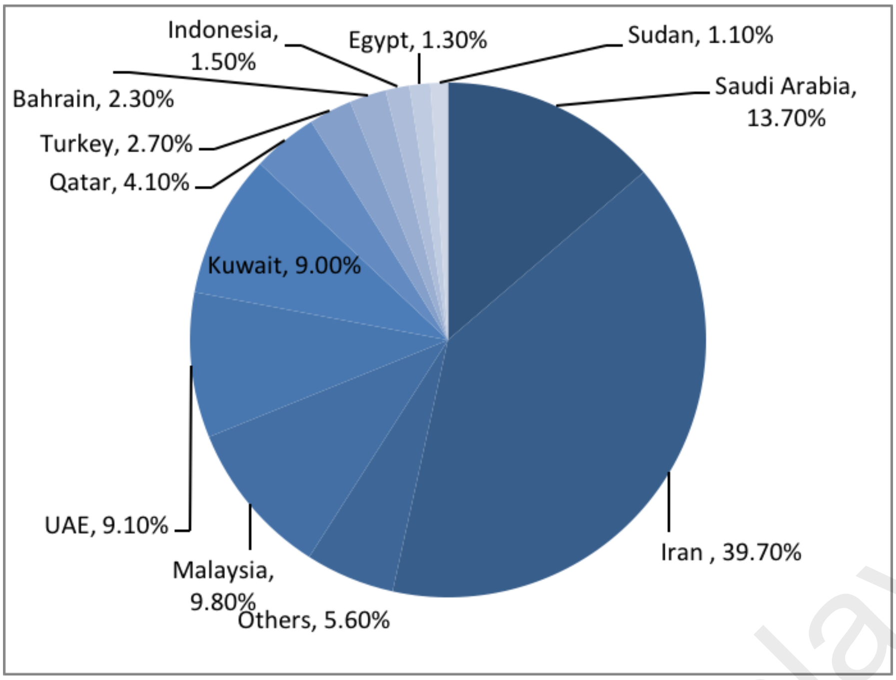
In the Economic Report 2012/2013 by the Ministry of Finance,[505] the Islamic banking business was stated to have continued to expand in the first seven months of the year 2012 with a total asset increasing 20.60% to RM469.5 billion, representing 24.2% of the country's banking system's assets. In 2011, it expanded by 24.1% to RM436.1 billion, reflecting 23.7% of the total banking system assets.

In comparison to Islamic banking shares around the world, Malaysia is ranked third with asset worth of 9.80 percent shares presented in the global Islamic banking asset, lagging behind the Kingdom of Saudi Arabia (13.70%) and the Islamic republic of Iran (39.70%). The following chart shows the percentage of Islamic banking shares around the world:

Chart 7.1: Islamic Banking Shares around the world

[504] Malaysia Government website of Economic Transformation Program, "EPP 10: Becoming the Indisputable Global Hub for Islamic Finance," retrieved on 17 September 2013, http://etp.pemandu.gov.my/Financial_Services-@-Financial_Services_-_EPP_10-;_Becoming_the_Indisputable _ Global_Hub_for_Islamic_Finance.aspx.

[505] Ministry of Finance Malaysia, *Economic Management and Prospect: Economic Report 2012/2013*, 5.



Source: Central Banks, Individual institutions, the Banker

The initiative to increase Malaysia's Islamic banking asset provides a positive sign as it is important for Malaysia to become as an undisputable Islamic banking and finance global hub.

In terms of *Takaful* industry, Malaysia's *takaful* insurance industry still has plenty of room for growth due to several factors including a low penetration rate despite a pre-dominant Muslim population. "The *Takaful* penetration rate in 2010 was between 10% and 11%," said an analyst with OSK Research. "With a nation of 17 million Muslims, there is a huge potential for growth.[506]

Syarikat *Takaful* Malaysia Bhd. Group managing director Datuk Mohamed Hassan Kamil concurred that the penetration rate was still low at 10% compared to conventional insurance, which was reported to be close to 43%.[507] In 2012, *takaful* market share was only 10% from the total number of 22% Islamic finance share in Malaysia.[508]

---

[506] The Edge, "Takaful Industry has Right Ingredients to Grow," retrieved on 16 October 2012, http://203.115.229.228/edgemyjoomla/in-the-financial-daily/211802-takaful-industry-has-right-ingredients-to-grow.html.
[507] *Ibid.*
[508] The World Takaful Report, *Industry Growth and Preparing or Regulatory Change*, 19.

As reported in Ernst and Young World *Takaful* Report 2011; the conventional insurers have produced far better results than their *takaful* counterparts in terms of return on equity, which was based significantly on their investment returns whereas *Takaful* returns have recovered after a slight fall during the financial crisis.[509]

Therefore, *Takaful* operators need to be creative in introducing new marketing strategies in promoting their products. Besides opening more outlets, within Malaysia and beyond ASEAN, new distribution channels such as tele-marketing, direct marketing, e-marketing should be aggressively employed. Looking at the global Muslim market, it is quite clear that insurance penetration is lagging behind, averaging around US$17 per person. It is obvious that if new and innovative marketing strategies are used, then it is possible to reach this market.[510]

7.2.6 Malaysian Islamic Finance Institution in Global

Currently, there is no local Islamic bank opening their subsidiary abroad. However, local conventional bank and the largest one in Malaysia, Maybank, has played an active initiative at the international level and had opened its branches in over 16 countries, namely Bahrain, Brunei, Cambodia, China, Hong Kong, India, Indonesia, Myanmar, Pakistan, Papua New Guinea, Philippines, Singapore, Thailand, USA, United Kingdom and Vietnam.[511] In Indonesia, Maybank had opened Maybank Syariah Indonesia and it could be considered as expanding local Islamic banks regionally, but not internationally. Perhaps, this could be considered as a pioneering effort in expanding local Islamic banks out of Malaysia due to Maybank's experiences in operating Islamic banking in its subsidiary in Malaysia, namely the Maybank Islamic. Another Malaysia's domestic conventional bank like CIMB bank has opened its branches in over 10

[509] Ernst and Young, *The World is Bumpy: Globalization and New Strategies for Growth,* 34.
[510] Yon Bahiah Wan Aris,"Takaful – An Option to Conventional Insurance: A Malaysian Model," 4.
[511] Maybank Website, "Banks Around The World," retrieved on 7 February 2013, http://www.relbanks.com/asia/malaysia/cimb-group/branches.

countries, namely Bahrain, Brunei, Cambodia, China and Hong Kong, Indonesia, Myanmar, Singapore, Thailand, United Kingdom and USA.[512] Other than these, there are no other Islamic banks in Malaysia that have opened their business internationally. Bank Islam, as the first Islamic Bank in Malaysia, is also focusing on local banking business and there is no sign for the Bank to operate internationally. There is no Malaysian bank that has ventured in the Middle East such as in Bahrain, Qatar, Saudi Arabia and U.A.E. The most probable reason is that they are all city states and they are well banked. The opening of new branch in other country does not give any meaning if the bank could not be competitive.

One investment Banker based in Hong Kong stressed in an interview "If you are one of the big banks you need a presence in New York, London and Hong Kong – you cannot claim to be global otherwise."[513]

7.2.7 Global Hub Impact

Malaysia had liberalized its Islamic finance services to foreign financial providers and as in 2009 the Central Bank of Malaysia had approved six licenses to foreign Islamic banks. Currently, there are healthy competitions between local and foreign Islamic finance institutions in providing the best services to the Malaysian customers. However, in the near future, a secure plan must be designed to rescue affected local Islamic financial institutions from this competition. Current policy allows foreign Islamic bank to provide Islamic banking retail services to domestic customers, where this type of banking services is the core business to local Islamic banks. The current study found that Maybank Islamic bank remains as the top of local Islamic banks while HSBC Amanah as a foreign Islamic bank positioned at number five lagging behind three other local Islamic banks, namely Alliance Islamic bank, AmIslamic and RHB Islamic. However, HSBC Amanah surpassed other seven local Islamic banks, namely

[512] *Ibid.*
[513] Long Finance of Z/Yen Group, *The Global Financial Centres Index 11*, 28.

Hong Leong Islamic bank, Affin Islamic bank, Public Islamic bank, EONCap Islamic bank, Bank Muamalat, Bank Islam and CIMB Islamic.

The liberalization and a more open policy by the Malaysian financial authority approved in a study conducted by Sok-Gee Chan and Mohd Zaini Abd Karim.[514] They found that foreign banks in Malaysia are more efficient as compared to those in other countries in the ASEAN region, which this might be due to the relatively high economic freedom in Malaysia over the years. Trade restriction in Malaysia is also relatively less compared to the other countries.

A "Rescue Package" must be in the authority's plan to secure local Islamic financial institution affected in the competition with foreign Islamic banks. The permissibility license for foreign Islamic banks to provide service in retail banking sector will affect local Islamic banks, which earn profit from such business. The purpose of the establishment of foreign Islamic banks must be strictly obvious not to affect domestic business and their business should be in international segments by providing financial services to international customers. The Central Bank of Malaysia had issued six licenses for foreign banks, namely Al-Rajhi Banking and Investment Corporation (Malaysia) Berhad, Kuwait Finance House (Malaysia) Berhad, Asian Finance Bank Berhad, HSBC Amanah Malaysia Berhad, OCBC al-Amin Bank Berhad and Standard Chartered Saadiq Berhad. Among the effects of foreign bank's entry are, they may reduce charter values of domestic banks, in particular by increasing competition and thereby lowering the profits of domestic banks, making them more vulnerable. This may have a destabilizing effect on the financial system, especially if the domestic prudential regulations and supervision are not strong. Therefore, the Central Bank of Malaysia needs to pay attention to ensure that adequate regulation and supervision is adopted in securing local Islamic banks.

---

[514] Sok-Gee Chan and Mohd Zaini Abd. Karim (2011), "Efficiency of Foreign Banks: Evidence from Selected (Association of Southeast Asian Nations," *ASEAN Countries, African Journal of Business Management*, (Vol. 5 (14), 2011), 5617-5626.

7.2.8 Positioning Malaysia as a Center for Islamic Finance

To become an Islamic finance global hub, Malaysia must be positioned as a centre for all Islamic finance factors. Thus, the country must confirm to transform as a centre for the following subjects:

7.2.8.1 Centre of Human Resources and Talent Development

7.2.8.2 Centre of Product Development and Innovation

7.2.8.3 Centre of *Sharī'ah* Deliberation and Reference

7.2.8.4 Centre of Islamic Fund Flows

7.2.8.5 Centre of Ancillary Services (Legal, Accounting and Processing Services / Outsourcing Services)

7.2.8.6 Centre of Islamic Capital and Money Market

7.2.8.7 Diversity of Islamic Finance Players

7.2.8.8 Domestic Islamic Finance Institution (Banking, *Takaful* and Islamic Capital Market) with global linkages

7.2.8.9 International Islamic Finance Institutions presence in Malaysia

BIBLIORAPHY

1. ACTS

Central Bank Act 2009, Law of Malaysia, (Act 701).

Federal Constitution 1957.

Islamic Banking Act 1983.

Laws of Malaysia, Takaful Act 1984.

Securities Commission Act 1993 (ACT 498).

2. BULLETINS

Accountants Today, *Prospects for Accountants in Islamic Finance*, Malaysian Institute of Accountants, July/August 2012, Vol. 25 No.4, 2012.

Securities Commission of Malaysia, *Malaysia's Experience in Developing the Islamic Capital Market and Its Growth Potential*, Bi Annual Bulletin of Malaysian Islamic Capital Market, Jan-June 2012, Vol. 7, No.1, (Kuala Lumpur, Malaysia: Securities Commision, 2012).

3. BOOKS

Ab Mumin Ab Ghani dan Fadillah Mansor (eds). (2006). *Dinamisme Kewangan Islam di Malaysia*. Kuala Lumpur: Penerbit Universiti Malaya.

Abdulazeem Abozaid et al. (2008). *Islamic Capital Markets; Products, Regulation & Development*. Jeddah, Saudi Arabia: Islamic Research and Training Institute.

Ahsene Lahsasna and M. Kabir Hassan et al. (2011). *Islamic Capital Markets: Products and Strategies*. United Kingdom: John Wiley and Sons, Ltd.

Akademi Pengajian Islam Universiti Malaya (2001). *Buku Panduan Penulisan Tesis/Disertasi Ijazah Tinggi Akademi Pengajian Islam*. Kuala Lumpur: Akademi Pengajian Islam Universiti Malaya, Lembah Pantai.

Ali Adnan Ibrahim et al. (2008). *Islamic Capital Markets; Products, Regulation & Development*. Jeddah, Saudi Arabia: Islamic Research and Training Institute.

Bank Negara Malaysia (2001). *Financial Sector Master Plan*. Kuala Lumpur: Bank Negara Malaysia.

___________________(2015). Global Sukuk Report 1Q2015. Kuala Lumpur, Malaysia: Bank Negara Malaysia.

___________________(2010). *MIFC: Malaysia: Your Business Connection To Global Islamic Finance*. Kuala Lumpur, Malaysia: Bank Negara Malaysia.

___________________ (2007). *Shariah Resolution of Bank Negara Malaysia*, 1st Edition. Kuala Lumpur, Malaysia: Bank Negara Malaysia.

___________________(1999). *The Central Bank and the Financial System in Malaysia*, Kuala Lumpur: Bank Negara Malaysia.

Bearden, W.O, Netemeyer, R.G.(1999). *Handbook of Marketing Scales-Multi Item Measures for Marketing and Consumer Behavior Research*. Thousand Oaks, California: SAGE Publications, Inc.

Buckley, P.J. and M. Casson (1991). *The future of the Multinational Enterprise*. London: Mcmillan.

Cavana, R.Y., Delahaye, B.L., & Sekaran U. (2001). *Applied Business Research: Qualitative and Quantitative Methods.* Australia: John Wiley & Sons Australia. Ltd.

Cresswell J.W.(2005). *Educational Research – planning, conducting and evaluating quantitative and qualitative research*, Ed.2. New Jersey: Pearson Merril Prentice Hall.

CIMB ISLAMIC (2015). Malaysia Islamic Finance Report 2015. Kuala Lumpur, Malaysia: CIMB ISLAMIC.

D. Arner (2007). *Financial Stability, Economic Growth and the Role of Law*. United Kingdom: Cambridge University Press, Chapter 2.

D. Beim & C. Calomiris (2001). *Emerging Financial Markets*. London: Mcgraw Hill.

David Brian Dewitt and Carolina G. Hernandez (2003). *Development and Security in Southeast Asia: Globalization,* Vol.3. England: Ashgate Publishing Limited.

Deloitte (2011). *The Deloitte Islamic Finance leaders survey in the Middle East: Benchmarking Practices*. United Kingdom: Deloitte and Touch (M.E.).

Department of Islamic Development Malaysia (2007). Tafsir ar-Rahman Interpretation of the Meaning of the Quran. Putrajaya, Malaysia: Department of Islamic Development Malaysia.

Earl Babbie (2001). *The Practice of Social Research,* 9th Edition. United States of America: Wadsworth.

Economist Corporate Network (2010). *The Global Outlook of the Islamic Finance Services Industry: An Economist Corporate Network Brief*. Singapore: The Economist Intelligent Unit Ltd.

Ernst & Young (2012) *The World is Bumpy: Globalization and New Strategies for Growth*. United Kingdom: Ernst & Young Global Limited.

Field, A.(2009). *Discovering Statistics Using SPSS.* (3rd ed.). London: SAGE Publications Ltd., 2009.

Graciela Laura Kaminsky and Sergio Schmukler (2008). *Short-run Pain, Long-Run Gain: The Effects of Financial Liberalization*. United Kingdom: Oxford University Press.

Geoffrey Jones (1992). *Banks as Multinationals*. London: Routledge Publication.

George, D. & Mallery, P.(2001). *SPSS for Windows Step by Step: A Simple Guide and Reference,* 10.0 Update, (3rd ed.). Canada: Allyn and Bacon.

Gibbons, M. et al.(1998). *The Globalization of Higher Education*. Buckingham, UK: The Society for Research into Higher Education and Open University Press.

Hair, J.F., Black, W.C., Babin, B.J. & Anderson, R.E.(2010). *Multivariate Data Analysis*. Delhi, India: Pearson Education Inc.

Hamim S. Ahmad Mokhtar, Naziruddin Abdullah & Syed M. Alhabshi (2008). *Efficiency and Competition of Islamic Banking in Malaysia.* United Kingdom: Emerald Grouping Publishing Limited, Vol. 24 No.1.

Hassan Scott Ordierno (2010). *Regulating Takaful, Islamic Finance News*. Kuala Lumpur, Malaysia: IFN Media Sdn. Bhd.

Hossein Askari, Zamir Iqbal, Noureddine Krichene, Abbas Mirakhor (2010). *The Stability of Islamic Finance: Creating a Resilient Financial Environment for a Secure Future*. Singapore: John Wiley and Sons (Asia) Pte. Ltd.

Hossein Askari, Zamri Iqbal and Abbas Mirakhor (2010). *Globalization & Islamic Finance: Convergences, Prospects & Challenges.* Singapore: John Wiley & Sons (Asia) Pte.Ltd.

Idris Awang (2001). *Kaedah Penyelidikan: Suatu Sorotan*. Kuala Lumpur: Intel Multimedia and Publication.

International Shari'ah Research Academy for Islamic Finance (ISRA) (2011). *Islamic Financial System: Principles and Operations*. Kuala Lumpur: International Sharia'h Research Academy for Islamic Finance.

Islamic Finance news (2011). *Malaysia: A Global hub for Islamic Finance*, Issuance: 15th June 2011. Kuala Lumpur: RedMoney.

____________________(2012). *Development, Growth and Challenges of Takaful in Malaysia*. Kuala Lumpur, Malaysia: Redmoney Group.

Islamic Financial Services Board (2009). *Guiding Principles on Shariah Governance System for Institutions Offering Islamic Financial Services*. Kuala Lumpur, Malaysia: Islamic Financial Services Board (IFSB).

____________________(2015). *Islamic Financial Services Industry Stability Report 2015.* Kuala Lumpur, Malaysia: IFSB.

J.W. Creswell and V.L. Plano Clark (2007). *Designing and Conducting Mixed Methods Research*. California: Sage Publications.

Jawatankuasa Tetap Bahasa Melayu (1992). *Pedoman Transliterasi Huruf Arab Ke Huruf Rumi*. Kuala Lumpur: Dewan Bahasa Dan Pustaka (DBP).

John A.Sonquist and William C. Dunkelberg (1997). *Survey and Opinion Research: Procedures for Processing and Analysis*. Eaglewood Cliffs, New Jersey: Prentice Hall.

John Urry (2000). *Sociology Beyond Societies, Mobilities for the twenty-first century*. London: Routledge Publication.

Kahn R.L. & Cannell, C.F.(1957). *The Dynamics of Interviewing: Theory, Technics and Cases.* New York: Wiley.

Kamal Khir, Lokesh Gupta and Bala Shanmugan (2009). *Islamic Banking: A Practical Perspective*. Selangor: Pearson Malaysia Sdn. Bhd.

Liamputtong, P. & Ezzy, D.(2005). *Qualitative Research Methods*. Victoria: Oxford University Press.

Lynch, B.K.(1996). *Language Program Evaluation: Theory and Practice.* New York: Cambridge University Press.

Malaysia Takaful Association and Ernst & Young (2015). *Malaysian Takaful Dynamics, Central Compendium 2015*. Kuala Lumpur, Malaysia: Malaysia Takaful Association and Ernst & Young.

Miles, M.B. & Huberman, A.M (1994). *Qualitative Data Analysis*, Ed. 2. Thousands Oaks: Sage Publications.

M.K. Lewis and K.T Davis (1987). *Multipliers and the Portfolio Approach: A Geometric Exposition*. Appendix to Domestic and International Banking, Philip Allan Publishers Ltd.

Mustapa Mohamed et.al.(2000). *Globalization: A Malaysian View* in Nik Mustapha Nik Hassan, et al. (ed), *The Economic and Financial Imperatives of Globalization: An Islamic Response*. Kuala Lumpur: IKIM.

Malaysia International Islamic Financial Centre (2008). *Primer to Islamic Finance*. Kuala Lumpur, Malaysia: Bank Negara Malaysia.

Malaysia International Islamic Financial Centre (2010). *The MIFC Community Directory: Connecting Business with Islamic Finance*, vol.2. Kuala Lumpur: Malaysia International Islamic Financial Centre.

Martin Albrow and Elizabeth King (1990). *Globalization, Knowledge and Society*. London: Sage Publications.

McMillan Publishers Ltd.(2008). *The New Palgrave Dictionary of Economics*, ed. 2nd, Vol. 1. New York: McMillan Publishers Ltd.

Mervyn K. Lewis (1999). *The Globalization of Financial Services: An Overview*, in *The Globalization of Financial Services*, ed. William G.Egelhoff, Paul W.Beamish, Joanne E.Oxley and Bernard Yeung, Chris Milner, James Foreman-Peck, Thomas L. Brewer, John Cantwell, Cheltenham, United Kingdom: Edward Elgar Publication.

Mian M. Nazeer (1981). *The Islamic Economic System: A Few Highlights*, Islamabad: Pakistan Institute of Development Economic Order.

Mohamad Najib (1999). *Penyelidikan Pendidikan.* Skudai: Penerbit Universiti Teknologi Malaysia.

Mohd Sheffied Abu Bakar (1987). *Metodologi Penyelidikan*. Kuala Lumpur: Dewan Bahasa Dan Pustaka.

Nixon, J. (1992). *Evaluating the whole Curriculum.* Philadelphia: Open University Press.

Organization for Economic Co-Operation and Economic Development (OECD) (1998). *Human Capital Investment: An International Comparison*. Paris, (OECD Publications.

Patton, M.Q.(1990). *Qualitative Evaluation and Research Method.* California: Sage Publications.

PricewaterhouseCoopers (2010). *Gateway to Asia; Malaysia, International Islamic Finance Hub.* Kuala Lumpur: PricewaterhouseCoopers.

____________________(2011). *Shariah Audit: Industry Insight*. Kuala Lumpur, Malaysia: Pricewaterhouse Coopers.

____________________(2008). *Malaysia, Asia's Islamic Finance Hub*. Kuala Lumpur, Malaysia: PricewaterhouseCoopers.

Puvenesvary, M.. Interviews. In Puvenesvary, M., Abdul Rahim, R., Sivabala Naidu, R., Badzis, M., Mat Nayan, N.F. & Abd. Aziz, N.H. (2008). *Qualitative Research: Data Collection & Data Analysis Techniques.* Sintok: UUM Press.

REDmoney (2011). *Islamic Finance News 2011 Guide*. Kuala Lumpur, Malaysia: REDmoney Publication.

_________ (2012). *Islamic finance News*. Kuala Lumpur: Redmoney Publications.

Saiful Azhar Rosly (2005). *Critical issues on Islamic Banking and Financial Markets: Islamic Economics, Banking and Finance, Investments, Takaful and Financial Planning*. Kuala Lumpur, Malaysia: Dinamas Publishing.

Samuel P. Huntington (1998). *The clash of Civilizations and the Remarking of World Order*. London: Touchston Book.

Sekaran U. (2003). *Research Methods for Business: A Skill Building Approach*. USA: John Wiley & Sons, Inc.

Sidek Mohd Noah (2009). *Reka bentuk Penyelidikan Falsafah, Teori dan Praktis*. Serdang: Penerbit Universiti Putera Malaysia.

Standard and Poor's Rating Services (2010). *Islamic Finance Outlook 2010*. McGraw Hill.

Sudin Haron and Wan Nursofiza Wan Azni (2009). *Islamic Finance and Banking System: Philosophies, Principles and Practices*. Selangor, Malaysia: McGraw-Hill (Malaysia) Sdn. Bhd.

Syed Othman al-Habshi, et.al (2011). *An Introduction to Islamic Economics and Finance*. Kuala Lumpur: CERT Publication Sdn. Bhd.

The New Palgrave Dictionary of Economics, vol. 3, Second Edition (2008). New York: Palgrave Mcmillan Publishers Ltd.

Wahbah Zuhaili (1984). *Al-Fiqhul Islami Wa Adillatahu*, Vol. 4. Damsyik, Syria: Darul Fikri.

Y. Casis (2006). *Capitals of Capital: A History of International Financial Centres, 1780-2005.* United Kingdom: Cambridge University Press.

4. CONFERENCES

Alessandra Bonfiglioli, "How Does Financial Liberalization affect Economic Growth?," (Conference Paper No.736, Institute for International Economic Studies, Stockholm University, Sweden, 2005).

Azizan Abdul Rahman, "Creating An Effective and Efficient Regulatory Framework for the Islamic Capital Market," (Seminar paper presented at the Financial Regulators Forum on Islamic Finance, 2007).

Ernesto Aguirre, "Basic Reforms of the Banking Systems in Latin America: Comparative Analysis, Trends and Outlook," (Second International Conference on Reforms of the Banking Systems in Latin America), Caracas, Venezuela, October 1997).

Ismail Bin Abd Rahman and Melati Ahmad Anuar, "What Motivates Malaysian Banks to Go International? A Case of Islamic Banking Products," (8th International Conference on Islamic Economics and Finance, Doha Qatar, 19-21 December 2011).

James R. Barth, Luis G. Dopico, Daniel E.Nolle and James A. Wilcox,"An International Comparison and Assessment of the Structure of Bank Supervision," (Conference Paper, February 21, 2002).

Jhordy Kashoogie Nazar, "Regulatory and Financial Implications of Sukuk's Legal Challenges for Sustainable Sukuk Development in Islamic Capital Market," (8th International Conference on Islamic Economics and Finance, Doha, Qatar, 2011).

Monzer Kahf, "Basel II: Implications for Islamic Banking," (International Conference on Islamic Economics and Banking, Jakarta, Nov. 22-24 2005).

Muhamad Muda, Abdullah Jalil, "Islamic Financial Product Development: Shariah Analysis," (IIUM International Conference on Islamic Banking and Finance (IICiBF) 2007).

Noor Hasyimah Sulaiman and Noor Hasiah Sulaiman (2009), "Analisis Prestasi Dan Kecekapan system Perbankan Islam di Malaysia Dari 2005-2007," (Seminar Ekonomi Islam Peringkat Kebangsaan 2009, 10-11 Februari 2009), Akademi Pengajian Islam, Universiti Malaya, Kuala Lumpur, 2009).

Omar A. Oseni, "Dispute Resolution in Islamic Banking and Finance: Current Trends and Future Perspectives," (Paper presented at the International Conference on Islamic Financial Services: Emerging Opportunities for Law/Economic Reforms of the Developing Nations 6-8 Oktober, 2009, University of Ilorin, Kwara State, Nigeria).

Rosylin Mohd Yusoff, Mohammed al-Wosabi and M.Shabri Abdul Majid, "Monetary Policy Shocks and Islamic Banks' Deposits in A Dual Banking System: A Comparative Analysis Between Malaysia and Bahrain," (8th Global Conference on Business & Economics, Florence, Italy, 2008).

Zeti Akhtar Aziz, Islamic Banking and Finance: Progress and Prospects Collected Speeches: 2000-2006, (Kuala Lumpur: Bank Negara Malaysia, 2006).

_____________, "The New Islamic Finance Landscape," (Keynote Address by the Governor of Bank Negara Malaysia, presented on 15th November 2011 at Sasana Kijang, Kuala Lumpur).

5. GUIDELINES

Guidelines on the Offering Structured Product, Securities Commission of Malaysia, Revised Edition: 27 April 2007.

6. JOURNALS

.

Agil Natt, Syed Othman al-Habshi, Mohd Pisal Zainal (2009). A Proposed Framework in the Human Capital Development in the Islamic Financial Services Industry. *The Journal of knowledge Economy & Knowledge Management 2009*, Vol.1, Spring.

Ahmet Selçuk DİZKIRICI, (2012). Considering Istanbul As A Financial Center: Targets, Following Steps. *Journal of Business and Social Science*, Vol.3 No. 18.

Ahmad Shukri Yazid, Juliana Arifin, Mohd Rasid Hussin and Wan Norhayate Wan Daud (2012). Determinants of Family Takaful (Islamic Life Insurance) Demand: A Conceptual Framework for a Malaysian Study International. *Journal of Business and Management,* Vol. 7, No. 6.

Alexandra Hennessy (2014). Redesigning Financial Supervision in the European Union. *Journal of European Public Policy*, Vol.21, No.2.

Aneta B. Spendzharova (2010). Multi-level Governance of Banking Regulation in the EU: Evidence from Developing Bank Supervision in Bulgaria and Hungary. *European Integration*, Vol.32, No.3.

Anichul Hoques Khan and Hasnat Dewan (2013). Who Should Supervise Banks for the Banking Sector Stability?. *Applied Economic Letters*. Vol.20, No.17.

Anindya K. Bhattacharya (2011). The Feasibility of Establishing an International Financial Center in Shanghai. *Journal of Asia-Pacific Business*, 12.

Asyraf Wajdi Dusuki (2010). Do Equity-Based Sukuk Structures in Islamic Capital Markets Manifest the Objectives of Shariah. *Journal of Financial Services Marketing*. McMillan Publishers Ltd, vol.15,3,203-214.

______________, and Abdelazeem Abozaid (2008), Fiqh Issues in Short Selling as Implemented in the Islamic Capital Market in Malaysia. *Journal of King Abdul Aziz University Islamic Economics*, Vol. 21, Number 2.

Asif Ahmed Qureshi (2011). Analyzing the Shariah Compliant Issues Currently Faced by Islamic Insurance. *Interdisciplinary Journal of Contemporary Research in Business*, Vol.3, No.5.

Ayman Zerban, Eslam H. Elkady and Rafik F. Omar, (2012). Islamic Finance and Global Financial Crises: How To keep Finance on Track, Topics in Middle Eastern and North African Economies. *Electronic Journal, Middle East Economic Association and Loyola University Chicago*, Vol.14.

Bekaert, Geert, Campbell R. Harvey and Christian Lundblad (2005). Does Financial Liberalization Spur Growth?. *Journal of Financial Economics,*Vol. 77, no. 1.

David R.Meyer (2011). Small-World job Mobility Integrates Hong Kong with Global Financial Centers. *Asian Geographer* Vol.28, No. 1.

Ewald Engelen and Anna Glasmacher (2013). Multiple Financial Modernities, International Financial Centers, Urban Boosters and the Internet as the Site of Negotiations. *Regional Studies*, Vol. 47, No.6.

Fakihah Azahari (2009). Islamic Banking: Perspectives on Recent Case Development. *Malayan Law Journal*.

Fatma Zehri and Najya AL-HERCH (2013). The Impact of the Global Financial Crisis On The Financial Institutions: A Comparison Between Islamic Canks (IBs) and Conventional Banks (Cbs). *Journal of Islamic Economics, Banking and Finance* (JIEBF), Vol.9, No.3.

Frederick V.Perry, J.D and Scheherazade S. Rehman (2011). Globalization of Islamic Finance: Myth or Reality?. *Journal of Humanities and Social Science*, Vol.1 No.9.

Gerald A.McDermott (2007). Politics, power, and institution building: Bank crises and supervision in East Central Europe. *Review of International Political Economy*, 14:2 May.

Herman E. Daly (1999).Globalization Versus Internationalization – some implications. *Journal of Ecological Economics 31*, Elsevier Science.

Julius B. Bertillo, Josefina B. Salindo and Florabel O. Nieva, (2013), "Global Impact of Financial Systems in the Arab World," *Sosial Science and Research Network*, Available at: "http://papers.ssrn.com/sol3/papers. cfm?abstract_id=2287415."

Kaminsky, Graciela and Sergio Schmukler (1999). The Twin Crises: Causes of Banking and Balance-of-Payments Problems," *American Economic Review*, 89 (3).

Landrum, R.E. (2005). Core Terms in Undergraduate Statistics. *Journal Teaching of Psychology*, (32 (4).

Levine, Ross (2001). International Financial Liberalization and Economic Growth. *Review of International Economics.*

M. Mansoor Khan, M. Ishaq Bhatti (2008). Islamic banking and finance: On its way to globalization. *Emerald Journal*, Emerald Group Publishing Limited, Vol.34, No. 10.

Mark. P. Hampton (1994). Treasure Islands or Fool's Gold: Can and Should small Island Economies copy Jersey. *Journal of World Development*, Vol. 22, No.2, Elsevier Ltd.

Mercy A. Kuo (2009). Islamic Finance in Southeast Asia: Strategic Context and Trends. *Journal of Islamic Economics, Banking and Finance,* (JIEBF), (Vol. 5, No.3, September – December 2009, Bangladesh: Islami Bank and Training and Research Academy (IBTRA)).

Metthew Donaghy and Michael Clarke (2010). Multi-Level Governance of Banking Regulation in the EU: Evidence from Developing Bank Supervision in Bulgaria and Hungary. *European Integration*, Vol.32, No.3.

Mohammad Mahbubi Ali (2012). Stockbroking in Islam: A Review of Literatures and Its Future Development in Malaysia. *Business & Management Quarterly Review*, 3(3), 1-8, 2012.

Mohamad Abdul Hamid, Noor Inayah Yaakub, Wan Kamal Mujani, Mohamed Sharizam and Kamaruzaman Jusoff (2011). Factors Adopting Islamic Home Financing: A Case Study Among Consumers of Islamic Banks in Malaysia. *Middle-East Journal of Scientific Research* 7 (Special Issue of Diversity of Knowledge on Middle East, IDOSI Publications.

Mohammad Salim al-Rowashdah (2009).The Political and Financial Implications of Globalization on the Islamic Banking: Facts and Events. *European Journal of Social Sciences*, Volume 12, Number 2.

Muhammad Hanif (2011). Differences and Similarities in Islamic and Conventional Banking. *Journal of Business and Social Sciences,* Vol. 2, No.2, February 2011.

Norafifah Ahmad and Sudin Haron, "Perception of Malaysian Corporate Customers Towards Islamic Banking Products & Services," *International Journal of Islamic Financial Services*, Vol. 3, Num. 4, (T.T)).

.Norhashimah Mohd Yasin (2001). Islamic Banking in Malaysia: Legal Hiccups and Suggested Remedies. *IIUM Journal*, Vol.9, No.1.

Ong Tze San, Lim Yee Theng and The Boon Hong (2011). A Comparison on Efficiency of Domestic and Foreign Banks in Malaysia: A DEA Approach. *Business Management Dynamics Journal*, Vol.1, No.4, Oct 2011.

Qiang Zhang and Gui Rong She (2008). Is there any Effect of Market Discipline on China’s Bank Supervision?. *Journal of Economic Policy Reform*, Vol.11, No.1, March 2008.

Philip Arestis and Howard Stein (2005). An Institutional Perspective to Finance and Development as an Alternative to Financial Liberalization. *International Review of Applied Economics*, Vol.19, no.4, October 2005.

R. Ibrahim Adebayo and M. Kabir Hassan (2013). Ethical Principles of Islamic Financial Institutions. *Journal of Economic Cooperation and Development*, Vol. 34. No.1, Turkey: Statistical Economic and Social Research and Training Centre for Islamic Countries, 2013.

Rashidah Abdul Rahman, Siti Balqis and Faizal Dean (2013). Assessing the Risk Management Practices of Islamic Banks: Empirical Evidence from Malaysia and Pakistan. *Journal of Islamic Economics, Banking and Finance* (JIEBF), Vol.9, No.4, October-December 2013.

Razaleigh Muhamat @ Kawangit, Abdul Ghafar Don, Salasiah Hanin Hamjah, Fariza Md.Sham, Badlihisham Mohd.Nasir, Muhammad Faisal Asha’ari, Siti Rugayah Tibek, Zainab Ismail, Ideris Endot, Anuar Puteh, A’dawiyah Ismail, Mohd Zulkipli Abd Ghani (2012). The Management of Takaful Business Models in Malaysia. *Journal of Advances in Natural and Applied Sciences*, 6(4): 561-564.

Rosmi Yuhasni Mohamed Yusuf (2011). Revisiting and Redefining the Concept of Retakaful and the Viability of Its Model in Malaysian Takaful Industry. *Business Management Quarterly Review*, 2(4), Universiti Teknologi Mara, Melaka.

Samuel Mcphilemy (2013).Formal Rules versus Informal Relationships: Prudential Banking Supervision at the FSA Before the Crash. *New Political Economy*, Vol.18, No.5.

Saiful Azhar Rosli (2005). Islamic Banking: Doing Things Right and Doing Right Thing. *Malaysian Journal of Economic Studies.* Vol.XXXXII Nos. 1&2.

Shaista Wasiuzzaman and Hanimas-Ayu Bt Ahmad Tarmizi (2010). Profitability of Islamic Banks in Malaysia: An Empirical Analysis. *Journal of Islamic Economics, Banking and Finance*, Vol.6, No.4, October-December 2010.

Sok-Gee Chan and Mohd Zaini Abd. Karim (2011). Efficiency of Foreign Banks: Evidence from Selected (Association of Southeast Asian Nations," *ASEAN Countries, African Journal of Business Management*, Vol. 5 (14).

Stijin Claessens, Asli Demirgguc-Kunt and Harry Huizinga (2001). How Does Foreign Entry Affect Domestic Banking Markets?. *Journal of Banking and Finance*, Vol.25, Issue 5.

Wafica Ali Ghoul (2011). The Dilemma Facing Islamic Finance and Lessons Learned from the Global Financial Crisis. *Journal of Islamic Economics, Banking and Finance*, (JIEBF), (Vol. 7, No.1, January – March 2011, Islami Bank and Training and Research Academy (IBTRA), Bangladesh.

Yap Voon Choong, Chan Kok Thim and Bermet Talasbek Kyzy (2012). Performance of Islamic Commercial Banks in Malaysia: An Empirical Study. *Journal of Islamic Economics, Banking and Finance (JIEBF),* Vol.8, No.2, April-June 2012.

Zamri Bin Hassan (2002). Islamic Banking: Its legal Impediments and Reformation with Special Reference to Malaysia. *Law Majalla*, Vol. 1.

_____________, "Sharia Governance in Islamic financial institutions and the Effect of the Central Bank of Malaysia Act 2009," *Journal of International Banking Law and Regulation*.

7. NEWSPAPERS

Asmani, A., "Banks Get Green Light to Offer Another Islamic Product", *The Straits Times(Singapore)*, 13 June 2006.

Siow, L. S. , "Maybank Launches Islamic Banking", *The Business Times (Singapore),* 26 November 2005.

8. PRESENTATIONS

Ahmad Hizzad Baharuddin, "The Regulatory Framework of Islamic Financial System in Malaysia," (Director of Islamic Banking and Takaful Department of Bank Negara Malaysia's Presentation on 18 April 2011).

Mohd Razif Abdul Kadir,"Islamic Finance in Malaysia – Evolution & Current Development," (Deputy Governor of Bank Negara Malaysia, Presentation for MIFC Event on October 2009).

Baljeet Kaur Grewal, “Constraints on Growth of Islamic Finance,” (IFSB 4th Public Lecture on Financial Policy and Stability, Amman, Jordan, 2011).

Daud Vicary Abdullah (2011), “Growing Islamic Finance: Awareness, Education & Talent Development,” (Deloitte -SIDC Islamic Markets Programme 2011 -June,29 2011 –Kuala Lumpur, 2011).

9. PROCEEDINGS

Ahcene Lahsasna and Lee Sze Lin, “Issues in Islamic Capital Markets: Islamic Bond Sukuk,” (3rd International Conference on Business and Economic Research (3rd ICBER 2012) Proceedings, 12-13 March 2012, Golden Flower Hotel, Bandung, Indonesia, 2012).

M.A Muqtader Khan, “The Mythology of Islamic Economics and the Theology of the East Asian Economic Miracle,” (Proceedings of the Fourth Harvard University Forum on Islamic Finance: Islamic Finance: The Task Ahead Cambridge, Massachusetts, Center for Middle Eastern Studies, Harvard University, 2011).

Mohd Nordin Ngadimon et al., “Islamic Capital Markets: products, Regulation and Development,” (Proceedings of International Conference, Islamic Development Bank, Saudi Arabia, 2008).

Muhammad Al-Bashir Muhammad Al-Amin et al., “Islamic Capital Markets: Products, Regulation and Development,” (Proceedings of International Conference), Islamic Development Bank, Saudi Arabia, 2008).

Sudin Haron and Wan Norsafiza et.al., “Islamic Capital Markets: Products, Regulation and Development,” (Proceedings of International Conference), Islamic Research and Training Institute, Islamic Development Bank, Saudi Arabia, 2008).

Surianom Miskam, “Reference to The Shariah Advisory Council in Islamic Banking and Finance Cases: The Effect of the Central Bank of Malaysia Act 2009,” (Paper Proceeding in International Conference on Business and Economics Research (ICBER), at Hilton Hotel, Kuching Sarawak, 15-16 March 2010).

10. REPORTS

Bank Negara Malaysia, The Central Bank and the Financial System in Malaysia, (Kuala Lumpur: Bank Negara Malaysia, 1999).

IRTI, Resolution and Recommendations of the Council of the Islamic Fiqh Academy: 1985-2000, Islamic Development Bank, Jeddah, Saudi Arabia.

Long Finance of Z/Yen Group, The Global Financial Centers Index 10, (Qatar: Long Finance, 2011).

_________________________, The Global Financial Centres Index 11, Long Finance, (Qatar: Long Finance, 2012).

Mark Yeandle, Alexander Knapp, Michael Mainelli and Ian Harris, "The Global Financial Centres Index 3 (2007)," (City of London, Z/Yen Group Limited, 2008).

Ministry of Finance Malaysia, Economic Management and Prospect: Economic Report 2012/2013, (Malaysia: Ministry of Finance).

Monetary Authority of Singapore (MAS) Report 2006/2007 (2007), Monetary Authority of Singapore, Singapore.

Report of the Islamic Capital Market Task Force of the International Organization of Securities Commissions, "Islamic Capital Market Fact Finding Report," (OICV-IOSCO, 2004).

The World Takaful Report, Industry Growth and Preparing or Regulatory Change, (United Kingdom: The world Takaful Report and Ernst & Young, 2012).

11. RESEARCHES

Douglas W.Arner, "The Competition of International Financial Centres and the Role of Law", (University of Hong Kong, Research Grant HKU 7401/05H, 2007).

Sabir Mohammed Hassan, "Issues in the Regulation of Islamic Banking (The Case of Sudan)," (Research and Studies Series, Bank of Sudan, Khartoum, Sudan, 2004).

Swiss Re Sigma Study 2003: Axco Global Statistics 2005. Quoted in ‘Issues in Islamic Finance and (re) Takaful,’ PricewaterhouseCoopers.

12. SPEECHES

Eddie Yue, “Hong Kong’s Possible Role in Islamic Finance,” (Welcome address by Deputy Chief Executive of the Hong Kong Monetary Authority and Executive Board Chairman of the Treasury Markets Association, at the Hong Kong Showcase on Islamic Finance, Dubai and Amman, 11-12 May 2008).

Nik Ramlah Mahmood, “Malaysia Can Strengthen Its Position as Islamic Capital Market Hub,” (Keynote address at IFN 2011 Issuers and Investors Asia Forum, KL Convention Center, Kuala Lumpur, 2011).

Zamani Abdul Ghani, “Significant Trends Surrounding the Takaful Industry,” (Opening address at The 3rd International Convention on Takaful and Retakaful, Kuala Lumpur, 29th August 2007).

Zeti Akhtar Aziz , “Approaches to Regulation of Islamic Financial Services Industry,” (Governor of Bank Negara Malaysia-Speech at the IFSB Summit – Islamic Financial Services Industry and The Global Regulatory Environment- The Park Lane Hotel, London, 18 May 2004).

_______________, “Islamic Finance – Dynamic Industry in a Rapidly Changing Global Environment,” (Governor's Keynote Address at the 2nd International Islamic Finance Conference at Crowne Plaza Hotel, Dubai, U.A.E, 22 September 2003).

______________, “The New Islamic Finance Landscape,” (Keynote Address by the Governor of The Central Bank of Malaysia, presented on 15th November 2011 at Sasana Kijang, Kuala Lumpur).

________________, “Malaysia as an International Financial Centre,” (Keynote address by the Governor of Central Bank of Malaysia, at the dialogue with Industry participants on MIFC (Malaysia International Islamic Financial Centre, Kuala Lumpur, 1 November 2006).

________________, “Talent Development in Islamic Finance Over The Next decade,” (Keynote address by Dr Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia, at the Launching of IBFIM’s Islamic Finance Qualification Framework & Progression Route (IFQFPR), Kuala Lumpur, 14 December 2011).

________________,“The Challenge for a Global Islamic Capital Market – Strategic Developments in Malaysia,” (Keynote address by Dr Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia, at the Sukuk Summit 2007, London, 20 June 2007).

13. WEBSITES

Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), “Overview,” retrieved on 28 October 2011, http://www.aaoifi.com/aaoifi/TheOrganization/Overview/tabid/62/language/en-US/Default.aspx.

Arab News, “WikiLeaks bares US concern over London as Rival Financial Hub,” Arab News Website, retrieved on 23 February 2012, http://arabnews.com/economy/islamicfinance/article260047.ece

_____________, “Bond Issuers Turn to Malaysia, Asia,” retrieved on 10 October 2011, http://www.arabnews.com/node/394028.

_____________, “Hong kong Eyes Islamic Finance Product,” retrieved on 5 October 2011, www.arabnews.com/node/321247%3Fquicktabs_stat2%3D0+&cd=1&hl=en&ct=clnk&gl=myhttp://archive.arabnews.com/.

____________, “Kingdom gaining more clout in Islamic Finance,” retrieved on 30 Jan 20212, from http://arabnews.com/economy/islamicfinance/article569065.ece.

_____________, “Malaysia Pushing for Islamic Finance Legal Framework,” retrieved on 15 October 2011, http://arabnews.com/economy/islamicfinance/article208977.ece.

_____________, “Malaysia liberalizes financial sector for foreign players,” retrieved on 20 October 2011, http://archive.arabnews.com/?page=6&section=0&article= 122189&d=4&m=5&y=2009.

_____________,“Malaysia's Royal Award for Islamic Finance,” retrieved on 21 July 2011, http://www.bnm.gov.my/ index.php?ch=8&pg=14&ac=2090.

______________, Mushtak Parker: “Malaysia pushing for Islamic Finance Legal Framework,” http://arabnews.com/economy/islamicfinance/article208977.ece., 12 September 2011.

Bank Islam Malaysia Berhad, "Challenges in Developing Islamic Banking Operations," retrieved on 7 February 2013.

Bank Negara Malaysia, "Administered Legislation," Bank Negara Malaysia Website, retrieved on 5 July 2013, http://www.bnm.gov.my/index.php ?ch=en_legislation.

____________________, "BNM Guidelines," Bank Negara Malaysia Website, retrieved on 29 May 2013, http://www.bnm.gov.my /guidelines/03_dfi/03_ prudential/03_gl_ governance_of_shariah_committee.pdf.

____________________,"Guidelines on the Governance of Shariah Committee," retrieved on 26 October 2011, http://www.bnm.gov.my/ guidelines/01_banking/04_prudential_stds/23_gps.pdf.

____________________, "Law Harmonisation Committee," retrieved on 13 April 2016, http://www.bnm.gov.my/index.php?ch=260&pg=830&ac=861.

____________________, "Learn About the Bank," Bank Negara Malaysia Website, retrieved on 7 Jun 2013, http://www.bnm.gov.my/index.php?ch=7&pg=715&ac=802.

____________________, "List of licensed Banking institutions in Malaysia," retrieved on 18 November 2011, from http://www.bnm.gov.my/index.php?ch=13 &cat= banking&type=MB&fund=0&cu=0,

____________________, "Malaysian Takaful Industry 1984-2004," retrieved on 10 October 2012, http://www.bnm.gov.my/files/publication/tkf/ en/2004/booklet.en.pdf.

____________________, "Overview of Islamic Finance in Malaysia," BNM website, retrieved on 27 December 2011, http://www.bnm.gov.my/microsites/ financial/ 0204_ib_takaful.htm.

____________________, "Shariah Advisory Council of the bank," retrieved on 26 October 2011, http://www.bnm.gov.my/index.php? ch=7&pg=715&ac=802.

__________________, "Shariah Governance Framework," retrieved on 5 November 2011, http://www.bnm.gov.my/guidelines/ 05_shariah/ 02_Shariah_Governance_Framework_20101026.pdf.

___________________, "The Issuance of Shariah Parameter Reference 1 (Murabahah Parameter) to Promote Harmonisaton of Practice," retrieved on 12 August 2011, http://www.bnm.gov.my/index.php?ch=8&pg=14 &ac=1907.

_________________,"The Principles of Shariah in Islamic Finance: Shariah Standard on Mudarabah," retrieved on 10 April 2016, http://www.bnm.gov.my/ guidelines /05_ shariah/shariah_std_mudarabah.pdf.

Bernama.com, "Malaysia Ranks 28th in the Globalisation Index 2011," retrieved on 28 February 2012, http://www.bernama.com/bernama/ v6/newsbusiness. php?id=644627.

___________, "Malaysia To Enhance Efforts To Become Global Islamic Finance Hub" retrieved on 22 February 2012, http://finance.bernama.com/news. php?id=618391

Biz Daily, "Singapore Takes Third Spot on E&Y Globalization Index," retrieved on 28 February 2012, http://bizdaily.com.sg/newsite/ singapore-takes-third-spot-on-ey-globalisation-index/.

Bloomberg Businessweek, "Malaysian Islamic Banking Assets Rise 15 percent to $123 Billion," retrieved on 27 December 2011, http://www.businessweek.com/news/ 2011-10-07/malaysian-Islamic-banking-assets-rise-15-percent-to-123-billion.html.

Business Times, "Where is Malaysia's Mega Islamic Bank?, retrieved on 7 December 2011, http://www.btimes.com.my/Current_News/BTIMES/ articles/Babyx/ Article/index_html.

____________, "Mega bank, stock exchanges and trading platforms," retrieved on 26 September 2012, http://www.btimes.com.my/Current_ News/BTIMES/articles/ 20120424011119/Article/#ixzz250ZiD5YE.

Business Week, “Malaysian Islamic Banking Assets Rise 15% to $123 Billion,” retrieved on 7 October 2011, http://www.businessweek.com/news/2011-10-07/malaysian-islamic-banking-assets-rise-15 percent- to-123-billion.html.

Deloitte, “Understanding the Framework: Adopting the Basel II Accord in Asia Pacific,” retrieved on 4 February 2013, http://www.deloitte. com/ assets/ Dcom-Malaysia /Local%20Assets/Documents/02720_ Basel_II_Adopting_SCRN.PDF.

Emirates 247, “Mega Islamic Bank Maybe Launched 2013,” retrieved on 25 September 2012, http://www.emirates247.com /business/ mega/-islamic-bank-may-be-launched-in-2012-2012-02-22-1.444362.

Ernst & Young, “Financial Services Act 2013 and Islamic Financial Services Act 2013,” Ernst & Young Website, retrieved on 25 Jun 2013, http://www.ey.com/MY/en/Industries/ Financial-Services/Take-5-Volume-1_Financial-Services-Act-2013-and-Islamic-Financial-Services-Act-2013.

Global Takaful Group, “Critical issues Facing Takaful Operators With Special reference to Malaysia,” 16 October 2012. http://www.globaltakafulgroup.org/ sites/default/files/Syed%20Moheeb.%20Critical%20Issues%2022%20Nov%202011.pdf..

Gulf Business, “New $1Bn Islamic Bank in Doha,” retrieved on 22 September 2012, http://gulfbusiness.com/2012/04/new-1bn-islamic-bank-in-doha/#.UD74RpYs324.

Institut Bank-Bank Malaysia website, “The Malaysian Financial System,” retrieved on 10 April 2012, http://www.ibbm.org.my/v2/wp-content/uploads/ 2011/05/Chap-1-amended-010305_2305t060205.pdf.

International Center for Education in Islamic Finance (IFSA), Islamic Financial Services Act (FSA) and Financial Services Act (FSA) , INCEIF Website, retrieved on 6 April 2016, http://www.inceif.org/islamic-finance/islamic-financial-services-act-2013.

International Islamic Financial Market, “IIFM Profile,” retrieved on 27 October 2011, http://www.iifm.net/, 27 October 2011.

International Shariah Research Academy for Islamic Finance (ISRA), "International Shariah Audit Conference," retrieved on 1 November 2011, http://www.isra.my/events/events-calendar/details/5- international-shariah-audit-conference-2011-isac2011.html.

Islamic Banking Malaysia, "Legal and Regulatory Framework of Islamic Banking and Finance in Malaysia," Islamic Banking Malaysia Website, retrieved on 1 July 2013, http://islamicbanking-malaysia.com/legal-regulations/170-legal-and-regulatory-framework-of-islamic-banking-and-finance-in-malaysia.

Islamic Banking and Finance Institute Malaysia website, "Bank Negara to issue up to two mega Islamic bank licences" retrieved on 7 December 2011, http://www.ibfim.com/v2/index.php?option=com_ content&view= article&id=2957%3Aone-mega-islamic-bank-this-year&Itemid=179.

Islamic Capital Market, "History of Islamic Capital Market," retrieved on 12 November 2012, http://119.110.108.29:9117/255_ 216/Web/WebPage/History-of-Islamic-Capital-Market/History-of-Islamic-Capital-Markets.html. .

Kuala Lumpur Regional Centre for Arbitration, "Arbitration in Malaysia," retrieved on 26 October 2011, http://www.klrca.org.my/Arbitration-@-Arbitration _in_Malaysia.aspx.

Labuan Financial Services Authority, "Corporate Profile," retrieved on 28 October 2011, http://www.lfsa.gov.my/labuan-fsa-s-profile.

Malaysia's Government *Pemudah* Official Website, "Malaysia in the Global C Competitiveness Report 2011-2012," retrieved on 5 May 2012, http://www.pemudah.gov.my/c/document_library/get_file?p_l_id=11311 &folderId=178798 &name=DLFE-5102.pdf.

Malaysia Government website of Economic Transformation Program, "EPP 10: Becoming the Indisputable Global Hub for Islamic Finance," retrieved on 17 September 2013, http://etp.pemandu.gov.my/Financial_Services-@-Financial_Services_-_EPP_10-;_Becoming_the_ Indisputable _ Global_Hub_for_Islamic_Finance.aspx.

Malaysia Islamic Capital Market Webpage "History of Islamic Capital Market," retrieved on 6 January 2013, Malaysia International Islamic Financial Centre, retrieved on 20 October 2011, http://www.mifc.com/index.php?ch=seg_tal_pro&pg=seg_ tal_pro_ovr. Malaysia International Islamic Financial Center (MIFC), "Malaysia: Towards Global Retakaful Excellence," retrieved on 1 November 2013, http://www.mifc.com/index. php?ch=142&pg= 845&ac=704&bb=944.

______________________________, "Islamic Banking Act," retrieved on 10 Jun 2012, http://www.mifc.com/ index.php?ch=menu _law&pg=menu_law_rel&ac=55

.

______________________________, "Islamic Finance Talent Programmes," retrieved 10 November 2011, http://www.mifc.com/index.php?ch=seg_ tal_pro&pg=seg_tal_pro_ovr&ac=99&ms=2.

______________________________, "Shariah Advisory Council (SAC)," retrieved on 26 October 2011, http://www.mifc.com/index.php?ch=menu_ law&pg=menu_law_sac

Malaymailonline, "Bank Negara Isssues New Guidance to Tackle Uneven Islamic Finance Practices, retrieved on 10 April 2016, http://www.themalaymailonline.com /money/article/bank-negara-issues-new-guidance-to-tackle-uneven-islamic-finance-practices#sthash.S3kXKIaY.dpuf

Maybank Website, "Banks Around The World," retrieved on 7 February 2013, http://www.relbanks.com/asia/malaysia/cimb-group/branches.

Ministry of International Trade and Industry (MITI), "The Banking System in Malaysia," retrieved on 20 October 2011, http://www.miti.gov.my/ cms/content.jsp?id= com.tms.cms.section.Section_64594899-c0a8156f-5cff5cff-2b0aba2c.

Official website of the WEF "History", retrieved on 26 December 2013: http://www.weforum.org/history.

PricewaterhouseCoopers, "Islamic Finance in Malaysia," retrieved on 1 October 2011, http://www.pwc.com/my/en/issues/islamic-finance-malaysia.jhtml.

Securities Commission Malaysia "Liberalisation of Equity Holdings in Capital Market Intermediaries," retrieved on 8 December 2011, http://www.sc.com.my/ main.asp? pageid=754&menuid= &newsid=& linkid=&type=.

Shariah Fortune, http://shariah-fortune.com/component/content/article/6-standard/26-islamic-gold- investment-preserve-your-money, 18 August 2011.

The Edge, "Takaful Industry has Right Ingredients to Grow," retrieved on 16 October 2012, http://203.115.229.228/edgemyjoomla/in-the-financial-daily/211802-takaful-industry-has-right-ingredients-to-grow.html.

The Malaysia International Islamic Financial Centre (MIFC), "Introduction," retrieved on 27 October 2011, http://www.mifc.com/index.php?ch=menu_ exp&pg=menu_exp_ ovr&ac=37&ms=1.

The Star, "New Blue Print for Financial System Expansion Likely," retrieved on 20 September 2011, http://biz.thestar.com.my/ news/story.asp?file =/2009/8/6/business/4464176&sec=business.

_____________, "Mega Islamic Bank Will Set Benchmark," retrieved on 18 September 2012,http://biz.thestar.com.my/news/story. asp?file=/2012/6/25/ business/11543548&sec=business.

_____________, "One Mega Islamic Bank This Year," retrieved on 2 September 2012, http://biz.thestar.com.my/news/story.asp?file= /2010/10/27/business/ 7303314&sec=business.

______________, "Talent Shortage in Islamic Banking," retrieved on 2 October 2012, http://thestar.com.my/metro/story.asp?file=/2011/9/29/metroperak/9587530&sec=metroperak.

Z/Yen Official Website, "Financial Centers Futures: Small Ponds or Big Pools," retrieved on 25 March 2012, http://www.zyen.com/component/content/ article.html?id=236.

Zawya.com, "State of the Global Islamic Economy 2013 Report," retrieved on 23 February 2014, http://www.zawya.com/files/islamic-reports/tr-state-of-islamic-economy-2013.pdf.

14. WORKING PAPERS

Al-Jarhi, M and Iqbal M, "Islamic Banking: Answers to Some Frequently Asked Questions," (Occasional Paper No.4, Islamic Research and Training Institute, Islamic Development Bank, Jeddah, 2001).

Bonfiglioli, Alessandra and Caterina Mendicino, "Financial Liberalization, Banking Crises and Growth: Assessing the Links," (SSE/EFI Working Paper (No.567), 2004).

Carmine Di Noia and Giorgio Di Giorgio, "Should Banking Supervision and Monetary Policy Tasks Be Given to Different Agencies?," (Working Paper, October 19, 1999, Roma, Italy).

Charles Goodhart & Dirk Schoenmaker, "Should the Functions of Monetary Policy and Banking Supervision Be Separated ?," (Oxford Economic Papers, vol.47, n.4 (okt.1995).

Eduardo Lundberg, "Monetary Policy and Banking Supervision Functions on the Central Bank," (Brazil: Banco Central Do Brasil, Working Paper Series 2, Banco Central Do Brasil, Brazil, 2000).

Elisa Bain, Justin G. Fung and Ian R. Harper, "Multinational Banking: Historical, Empirical and Case Perspectives," (Melbourne Business School Working Paper, N.5,1999).

Grilli, Vittario and Gian Maria Milesi-Feretti, "Economic Effect and Structural Determinants of Capital Controls," (IMF Staff Papers, Vol. 42, No.3., 1995).

Habibullah Khan & Omar K.M.R. Bashar, "Islamic Finance: Growth and Prospects in Singapore," (U21 Global Working Paper Series, No. 001/2008).

International Monetary Fund, "Caribbean Centers, Stricter Rules Change Climate for Offshore Financial Centers," (in IMF Survey, vol.31, n.15, August, 2002).

Islamic Financial Services Board (IFSB) and International Association of Insurance Supervisors (IAIS), "Issues in Regulation and Supervision of Takaful (Islamic Insurance)," (Islamic Financial Services Board (IFSB) and International Association of Insurance Supervisors (IAIS) Working Paper Series, August 2006).

Juan Sole, "Introducing Islamic Banks into Conventional Banking System," (IMF Working Paper No. WP/07/175, 2007).

Kraay, Aart, "In Search of the Macroeconomic Effects of Capital Account Liberalization," (Working Paper of The World Bank Group, 1998).

Kun Ho Lee and Shakir Ullah, "Integration of Islamic and Conventional Finance," (International Review of Business Research Papers Vol.3, No.5 November 2005).

Luca Errico and Mitra Farahbaksh, "Islamic Banking: Issues in Prudential Regulations and Supervision," (International Monetary Fund Working Paper, 1998).

Richard S. Tedlow and Rawi Abdelal, "Theodore Levitt's The Globalization of Markets: An Evaluation after Two Decades," (Sosial Science Research Network Electronic Paper Collection (No. 03- 20), 2003).

Rodney Wilson,"The Development of Islamic finance in the UK," (Working Paper, Kuwait Programme on Development, Governance and Globalisation the Gulf States, 2009).

Rodrick, Dani, "Who Needs Capital-Account Convertibility?" (Contribution paper to a symposium edited by Peter Kenen, to be published as part of a Princeton Essay in International Finance Harvard University, Mimeo, 1998).

Rossidou-Papakyriacou E , "Internatioanl Co-Opeation in the Fight against Corruption from the point of view of an Off-shore Centre," (paper presented at the 4th European Conference of Specialized Services in the Fight against Corruption, Limassol (Cyprus), 20-22 October, 1999).

Tuya J. and Zamalloa L., "Issues on Placing Banking Supervision in the Central Bank," in Balino T. and Cottarelli C. (eds), Framework for Monetary Stability, (International Monetary Fund (IMF),1994).

Salman Syed Ali, "Introduction Islamic Capital Markets: Current State and Development Challenges," (Occasional Paper No.9, Islamic Research and Training Institute (IRTI), Jeddah, Saudi Arabia, 2008).

Sudin Haron, "Towards Developing a Successful Islamic Financial System: A Lesson from Malaysia," (Working Paper Series 003, 2004).

Wafik Grais and Matteo Pellegrini, "Corporate Governance and Shariah Complaince in Institutions Offering Islamic Financial Services," (World Bank Policy Research Working Paper 4054, 2006).

Yon Bahiah Wan Aris, "Takaful – An Option to Conventional Insurance: A Malaysian Model," (Working Paper, Faculty of Business and Management, University Technology MARA (UiTM)), Malaysia, 2004).

SUPPLEMENTARY

A. LIST OF PUBLICATIONS

1. Mohd Nazri Bin Mohd Noor, Mohammad Noorizzuddin Bin Nooh, Joni Tamkin Borhan (2014), The Global Hub Process: Malaysia's Vision Towards Becoming the Islamic Finance Global Hub Country, *International Journal of Business and Social Science*, (Vol.5, No. 8(1), July 2014).

2. Mohd Nazri Bin Mohd Noor, Joni Tamkin Borhan, Patmawati Binti Ibrahim, Mohammad Noorizzuddin Bin Nooh, Asmaddy Bin Haris, Muhammad Ridhwan Bin Ab. Aziz, Azrul Azlan Iskandar Mirza (2014), Malaysia Islamic Finance Global Hub: A Comparative Study Towards the Assessment Bodies in Reporting Global Hub Countries, *International Journal of Businessand Social Sciences*, (Vol.5, No.9, August 2014).

B. LIST OF PRESENTATIONS

1. Mohd Nazri Bin Mohd Noor, "The Role of Central Bank of Malaysia in Positioning Malaysia as a Global Hub for Islamic Finance," (The International Seminar on Research in Islamic Studies II (ISRIS II), University of Malaya, Kuala Lumpur, 15th -16th February 2012).

2. Mohd Nazri Bin Mohd Noor, "Understanding the Concept of Globalization and Financial Liberalization with the Highlight of Malaysia's Vision towards Islamic Finance Global Hub," (The First International Seminar on Malaysian-Thai Studies (ISMATS) 2012), Executive Development Centre (EDC-UUM), Universiti Utara Malaysia, Sintok, Kedah, Malaysia).