IMPACT OF *WAQF* FINANCING ON FEDERAL GOVERNMENT EXPENDITURE AND DEBT IN MALAYSIA

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ABSTRACT

Waqf was the provider of public goods, mixed public goods, and social services in Islamic history. In present economies, the goods and social services are provided by the government instead. These and other government expenditure components have caused burgeoning expenditure and excessive debt. In the case of Malaysia, the federal government has introduced the goods and services tax (GST) and reduced federal government expenditure to mitigate these issues. However, this strategy combination could cost welfare greatly. As such, this thesis aims to propose *waqf* as a means to finance certain Malaysian federal government expenditure and analyse its impact on federal government debt.

To achieve this aim, mixed methods research was employed. For the qualitative part, primary data were collected through semi structured interviews with *waqf* experts consisting of academicians, government officials, and industry players. Thematic analysis and interpretive method of analysis were then perform to identify the viability of the proposal, to come out with a model, and to investigate the resultant impact of this particular *waqf* implementation on federal government debt. In addition, input on the form of *waqf* capital and method to safeguard its perpetuity were also obtained from the mentioned methods of analyses to complete the theoretical model. The completed theoretical model forms a dynamic stochastic general equilibrium (DSGE) model for the quantitative part.

Data for the quantitative part was gathered from the literature, the Central Bank of Malaysia (BNM), and Public Mutual Berhad. These data helped determine the parameter values and some steady state values using ordinary least squares (OLS) method. Other steady state values were derived from the stationarised model equilibrium. To investigate

the resultant impact of *waqf* on federal government debt, the model equilibrium were subjected to simulation analysis.

The qualitative part of this thesis reveals that *waqf* financing certain federal government expenditure is doable because of political will, *Shari'ah* permissibility, and evidence of its implementation in the past. However, the application will not be without legal, management, financial, and public perception issues. Through partial centralisation of *waqf* laws, publication of *waqf* reports, revival of *waqf* deeds, human resource empowerment, and innovative *waqf* investment, those issues can be mitigated and model for *waqf* financing public expenditure be developed. Interviewees also agreed that federal government debt can be sustained through the means of this *waqf* application. Meanwhile, the quantitative part also showed that *waqf* financing public expenditure has an impact of reducing debt.

ABSTRAK

Wakaf merupakan penyedia barang awam, barang awam campuran dan perkhidmatan sosial dalam sejarah Islam. Dalam ekonomi semasa, barangan dan perkhidmatan sosial disediakan oleh kerajaan. Keadaan ini dan komponen-komponen perbelanjaan kerajaan yang lain telah menyebabkan perbelanjaan yang membebankan dan hutang terlampau. Di Malaysia, kerajaan pusat telah memperkenalkan cukai barang dan perkhidmatan (GST) dan mengurangkan perbelanjaan kerajaan pusat untuk menangani isu-isu ini. Namun demikian, kombinasi strategi ini mungkin akan merugikan kebajikan masyarakat dengan banyak. Oleh kerana itu, tesis ini bertujuan untuk menyarankan wakaf sebagai cara untuk membiayai perbelanjaan kerajaan Malaysia yang tertentu dan menganalisis impaknya terhadap hutang kerajaan pusat.

Untuk mencapai tujuan ini, kajian kaedah campuran telah digunakan. Untuk bahagian kualitatif, data primer telah dikumpulkan melalui temu bual separa berstruktur dengan pakar-pakar wakaf yang terdiri daripada para sarjana, pegawai kerajaan atau wakil industri. Analisis tematik dan analisis kaedah bertafsir telah dilaksanakan untuk mengenal pasti daya maju saranan itu, untuk memperkenalkan suatu model, dan untuk menyelidik hasil impak implementasi jenis wakaf ini terhadap hutang kerajaan pusat. Tambahan pula, input dalam bentuk modal wakaf dan kaedah untuk melindungi kekekalannya juga diperoleh daripada kaedah-kaedah analisis yang telah dinyatakan untuk melengkapkan model teori. Model teori yang lengkap ini membentuk model keseimbangan umum stokastik dinamik (DSGE) untuk bahagian kuantitatif.

Data untuk bahagian kuantitatif telah dikumpulkan daripada literatur, Bank Negara Malaysia, dan Public Mutual Berhad. Data-data ini telah membantu untuk menentukan nilai-nilai parameter dan beberapa nilai keadaan mantap dengan menggunakan kaedah kuasa dua terkecil (OLS). Nilai-nilai keadaan mantap yang lain diperolehi daripada model

keseimbangan yang pegun. Bagi menyelidik hasil impak wakaf ke atas hutang kerajaan pusat, model keseimbangan telah melalui analisis simulasi.

Bahagian kualitatif tesis ini telah memperlihatkan pembiayaan perbelanjaan kerajaan pusat yang tertentu melalui wakaf boleh dilaksanakan kerana kehendak politik, keizinan syariah, dan bukti implementasinya suatu ketika dahulu. Bagaimanapun, aplikasinya akan menimbulkan isu-isu perundangan, pengurusan, pembiayaan dan persepsi masyarakat. Melalui pemusatan separa undang-undang wakaf, penerbitan laporan-laporan wakaf, pemulihan usaha-usaha wakaf, pemerkasaan sumber manusia, dan pelaburan wakaf yang inovatif, isu-isu ini boleh ditangani dan suatu model untuk perbelanjaan awam melalui pembiayaan wakaf boleh dibangunkan.   Pihak-pihak yang ditemu bual juga bersetuju bahawa hutang kerajaan pusat boleh ditampung melalui cara aplikasi wakaf ini. Selain itu, bahagian kuantitatif juga menunjukkan bahawa pembiayaan perbelanjaan awam melalui wakaf mempunyai impak dalam mengurangkan hutang.

ACKNOWLEDGEMENTS

TABLE OF CONTENTS

CHAPTER 1: INTRODUCTION

CHAPTER 2: WAQF: CONCEPT, SHARI'AH, AND PRACTICE IN SELECTED COUNTRIES

CHAPTER 3: MALAYSIAN FEDERAL GOVERNMENT EXPENDITURE AND THE GROWING DEBT

CHAPTER 4: DATA AND METHODOLOGY

CHAPTER 5: QUALITATIVE ANALYSIS: *WAQF* FINANCING FEDERAL GOVERNMENT PUBLIC EXPENDITURE

CHAPTER 6: FINANCING SELECTED COMPONENTS OF FEDERAL GOVERNMENT EXPENDITURES

CHAPTER 7: QUANTITATIVE ANALYSIS: IMPACT OF WAQF FINANCING PUBLIC EXPENDITURE ON FEDERAL GOVERNMENT DEBT

LIST OF FIGURES

LIST OF TABLES

LIST OF SYMBOLS AND ABBREVIATIONS

δ :   Depreciation rate of capital

β :   Intertemporal discount factor

θ_0 :   Parameter of fiscal policy rule

θ_1 :   Parameter of fiscal policy rule

θ_2 :   Parameter of fiscal policy rule

φ :   Parameter of federal government expenditure per GDP

b :   Federal government debt to GDP

$\bar{b}$:   Steady state of federal government debt to GDP

B :   Federal government debt

C :   Consumption

$\bar{C}$:   Steady state of consumption

C^τ :   Total consumption

D :   Cash *waqf* return

$\bar{D}$:   Steady state of cash *waqf* return

G :   Federal government development expenditure

$\bar{G}$:   Steady state of federal government development expenditure

g	:	Federal government development expenditure to GDP
$\bar{g}$	:	Steady state of federal government development expenditure to GDP
I	:	Investment
$\bar{I}$	:	Steady state of investment
K	:	Capital
$\bar{K}$	:	Steady state of capital
L	:	Labour
$\bar{L}$	:	Steady state of labour
O	:	Leisure
R	:	Rental rate of capital
$\bar{R}$	:	Steady state of rental rate of capital
R^r	:	Interest rate
$\overline{R^r}$	:	Steady state of interest rate
$\hat{s}$	:	Primary balance to GDP
$\bar{\hat{s}}$	:	Steady state of primary balance to GDP
S	:	Savings
$\hat{S}$	:	Primary balance

t	:	At period t
$t\text{-}1$	:	At period $t\text{-}1$
$t\text{+}1$	:	At period $t\text{+}1$
T	:	Federal government revenue or tax
v	:	*Waqf* to GDP
$\bar{v}$	:	Steady state of *waqf* to GDP
V	:	*Waqf*
$\bar{V}$	:	Steady state of *waqf*
W	:	Wage
$\bar{W}$	:	Steady state of wage
y	:	Growth rate of GDP
Y	:	Final goods
$\bar{Y}$	:	Steady state of final goods
AH	:	After *Hijrah*
AMLA	:	Administration of Muslim Law Act
AR	:	First order autoregressive
BMMB	:	Bank Muamalat Malaysia Berhad

BNM	:	Bank Negara Malaysia or the Central Bank of Malaysia
BOT	:	Built Operate and Transfer
CGE	:	Computable general equilibrium
DFI	:	Development Finance International
DGE	:	Dynamic general equilibrium
DOSM	:	Department of Statistics Malaysia
DSGE	:	Dynamic stochastic general equilibrium
EAA	:	Egyptian *Awqaf* Authority
EPF	:	Employees Provident Fund
GCC	:	Gulf Cooperation Council
GDP	:	Gross domestic product
GE	:	General equilibrium
GII	:	Government investment issues
GLC	:	Government linked company
GST	:	Goods and services tax
IBA	:	Islamic Banking Act
ICT	:	Information and communications technology
IFRS	:	International Financial Reporting Standards

INTOSAI	:	International Organization of Supreme Audit Institutions
IPO	:	Initial public offering
IPTS	:	Institute of higher learning
IRF	:	Impulse response function
IT	:	Information technology
JAWHAR	:	Department of *Awqaf*, Zakat and Hajj
JCORP	:	Johor Corporation
KAPF	:	Kuwait *Awqaf* Public Foundation
KWAP	:	Kumpulan Wang Amanah Persaraan
LIBFC	:	Labuan International Business and Financial Centre
LIWF	:	Labuan International *Waqf* Foundations
MAIWP	:	Majlis Agama Islam Wilayah Persekutuan
MFRS	:	Malaysian Financial Reporting Standards
MGS	:	Malaysian government securities
MOF	:	Ministry of Finance
MUIS	:	Islamic Religious Council of Singapore
NAV	:	Net asset value
NC	:	New Classical

NK	:	New Keynesian
NLC	:	National Land Code
NPG	:	No Ponzi Game
OECF	:	Overseas Economic Cooperation Fund
OIC	:	Organisation of Islamic Cooperation
OLS	:	Ordinary least squares
PBUH	:	Peace be upon him
PERS	:	Private Entity Reporting Standards
PMB	:	Public Mutual Berhad
PWNS	:	Perbadanan Wakaf Negeri Sembilan
PWS	:	Perbadanan Wakaf Selangor
RBC	:	Real Business Cycle
REPO	:	Repurchase agreement
RO	:	Research objective
ROI	:	Return on investment
RQ	:	Research question
SAC	:	*Shari'ah* Advisory Council
SC	:	Securities Commission Malaysia

SIRC	:	State Islamic Religious Council
TSO	:	Third sector organisations
UM	:	University of Malaya
USIM	:	Islamic Science University of Malaysia
WANCORP:		Waqaf An-Nur Corporation Berhad
WSM	:	Wakaf Selangor Muamalat
YWM	:	Yayasan Waqaf Malaysia

LIST OF APPENDICES

CHAPTER 1: INTRODUCTION

1.1   Background of the Study

Waqf is a pious endowment in Islam that possesses significant economic potential. Due to religious and altruistic motives, *waqf* became the supplier of public goods, mixed public goods, and other related goods in Islamic history. It then emerged as a supplementary fiscal policy during the Ayyubid Dynasty. The value of *waqf* then steadily rose to a third of the Ottoman's fiscal revenue. In the context of current economy, the mentioned goods are mainly provided by the government to which government expenditures are incurred. Essentially, the goods make up the components of government public expenditure thus rendering *waqf* unnecessary.

However, burgeoning government expenditure puts a strain on government revenue which ultimately causes excessive borrowing. Excessive borrowing in turn causes unsustainable debt. This very issue has always been a major concern for every economy. Debt is only sustainable when government is able to pay for its current and future debt obligation and is usually assessed by observing the trend of debt to gross domestic product (GDP) ratio. A plethora of studies had been conducted to address unsustainable debt. Suggestions include investing in productive government expenditure, increase tax, reduce interest rate, and employing mix strategies. Upon learning the role of *waqf* as a supplementary fiscal policy in Islamic history, this thesis would want to examine this in light of current economy, specifically the current Malaysian economy.

Indeed, Çizakça (1998) envisioned that debt can be ultimately reduced should *waqf* be assigned to finance certain components of government expenditure. A simulation was specifically done for Malaysia by Mohd Umar, Shahida, Abdul Ghafar and Zaini (2012) which found that *waqf* can help government save more thus enabling the savings to finance debt. Hence the primary aim of this thesis is to investigate how *waqf* can finance certain Malaysian federal government expenditures (pure and mixed public goods as well

as other related goods) and analyse the impact of this particular *waqf* implementation on Malaysian federal government debt.

1.2   Problem Statement

The Malaysian federal government debt to GDP ratio is rising and this will bring negative consequences to the country. Motley (1987), Sutherland (1997), as well as Checherita and Rother (2010) found evidence that high government debt can cause contractionary effects. Teles and Mussolini (2014) showed how high debt to GDP ratio can constrain the effects of productive expenditures on growth in the long term. Kwon, McFarlane, and Robinson (2009) provided strong evidence that rising public debt can cause inflation in high indebted developing countries. Even the founder of Keynesian economics, John Maynard Keynes adopted a cautious view towards debt (Aspromourgos, n.d.). The Malaysian federal government had addressed this problem by introducing the goods and services tax (GST) and federal government expenditure reduction. However, the simultaneous tax increase and expenditure decrease have negative consequences on the Malaysian public welfare (Konzelmann, 2014).

On top of that, the steepest increase in Malaysian federal government debt to GDP ratio occurred at the same time with the steepest increase in primary deficit. These occurrences were during the aftermath of the 2008 global economic crisis which roughly suggests that external shocks affect federal government debt. External shocks can be difficult to predict and may occur now and then. The primary deficit is also an indication of burgeoning government expenditure. Moreover, the federal government debt to GDP ratio has crossed the 50% threshold in times where persistent primary deficit is already occurring. It is the intent of this study to find an effective solution.

Yet solutions stemming from conventional economics school of thought is already saturated. It is for this very reason that this research chose to look solutions from Islamic

economics. Islamic economics considers *waqf*, essentially a third sector component that has never been considered seriously in the public finance literature. Studies that build macroeconomic models to study debt sustainability very scarcely included the third sector in their modelled economy, inadvertently dismissing the impact that third sector could have on debt sustainability. This leaves a huge gap in the literature to which this study attempts to fill.

Meanwhile, studies done on the side of Islamic economics are vastly theoretical on the matter of *waqf*, debt sustainability, and public expenditures. Also, studies of *waqf* in the public finance field are mostly anachronistic. For instance, Faridi (1983) stated that Islamic economy consist of three sectors; public, private, and voluntary but did not frame them in light of modern economics. As a result, framework for *waqf* in current economies are lacking which pose difficulty to mathematically calculate the impact of *waqf* financing public expenditure on debt. Although Mohd Umar et al. (2012) did demonstrate how *waqf* can indirectly help the government to finance debt, the study done was without a theoretical framework. In fact, very few contemporary studies actually show this link between *waqf* and debt. This is expected because societies in modern economies mostly recognise the government as the provider of public goods through government spending. It is this research's motivation to fill that gap.

1.3   Research Objectives

This research studies the impact of *waqf* on Malaysian federal government debt when *waqf* finances public goods, mixed public goods, and other related goods. The related goods can also be termed as social services. Social services include elderly care and other vulnerable groups, flood prevention projects, river rehabilitation, and others. These goods also make up parts of the federal government expenditures (Ministry of Finance [MOF] Malaysia, 2010/2011). The federal government allocated budget to most Malaysian states

as *waqf* to provide for some of these goods. In addition, the private sector has also collaborated with the State Islamic Religious Councils (SIRCs) to take similar initiative. The Malaysian community too contributed *waqf* for the benefit of society.

To build a comprehensive understanding on the matter, this study firstly attempts to understand the workings of *waqf* in Malaysia to gather reasons for *waqf* financing public expenditures. It also seeks to understand the issues that may arise from that *waqf* implementation. By studying the issues, this thesis proceeds to develop a model for *waqf* financing public expenditure that Malaysia can adopt. Lastly, this thesis attempts to find out the impact of that *waqf* application on federal government debt. It must be duly noted that this research recommends *waqf* as a supplementary fiscal strategy and do not dismiss the role of tax and debt altogether. Below are this thesis's research objectives (ROs):

I.   To explore the extent to which *waqf* financing Malaysian federal government public expenditure is doable.

II. To propose a model of *waqf* financing federal government public expenditure for Malaysia.

III. To analyse the impact that *waqf* has on Malaysian federal government debt in the event that *waqf* finances Malaysian federal government public expenditure.

1.4   Research Questions

The research questions (RQs) of this study correspond to the ROs. To be specific, RQ1 and RQ 2 corresponds to RO 1, RQ 3 corresponds to RO 2, while RQ 4 corresponds to RO 3. The RQs are framed as follows:

I.   Why *waqf* financing Malaysian federal government public expenditure is doable?

II. What are the issues that could obstruct the use of *waqf* to finance Malaysian federal government public expenditure?

III. How can *waqf* finance Malaysian federal government public expenditure?

IV.   How will *waqf* impact Malaysian federal government debt in the event that *waqf* finances Malaysian federal government public expenditure?

1.5   Significance of the Study

This thesis argues that *waqf* can be an indirect solution to the Malaysian federal government debt problem by employing it to finance public expenditure. This thesis shows evidence that this implementation of *waqf* can be applied in Malaysia. Further, challenges as well as the way forward for this implementation of *waqf* are provided. As alluded in Section 2.0, there is a limited number of literature that addressed the topic of *waqf* in the public finance context thus exhibits the significance of this thesis. There are also positive implications beside from the literature gap. All of these are summed up as follows:

I.   This research made an effort to provide solutions to the Malaysian federal government debt problem which is in need of urgent and continuous attention.

II.   This research identifies the challenges and way forward for this particular implementation of *waqf* hence can be used as a reference by persons of authority in Malaysia and academicians worldwide.

III.   This research can also possibly be of use as reference by other countries intending to mimic this particular implementation of *waqf* which inadvertently adds on to the *waqf* literature.

IV.   This research establishes another solution to sustain debt aside from the typical conduct of fiscal and monetary policy. Since *waqf* originates from Islamic economics and related to the third sector economy, then this research has also introduced solutions to government debt problem from these fields.

V.   Following item IV, this research provides evidence on the significance of third sector role and Islamic economics.

VI.   This research contributes to the literature of *waqf* by helping to extend and argue the implementation of *waqf* outside of its traditional uses thus expounding the need of *waqf* in modern economy structure.

1.6   Organisation of the Study

This thesis is divided into eight chapters. Chapter 1, which is this chapter, serves as the introductory chapter that informs the research background and the research problem. ROs and RQs are also stated to make this research on point. Significance of this research is duly highlighted too.

Chapter 2 and Chapter 3 are the literature review chapters where the former focuses on *waqf* while the latter deals with public finance. Chapter 2 presents the Shari'ah of *waqf*, the application of *waqf* in public finance, the practice of *waqf* in Malaysia, and how *waqf* interacts within the Malaysian economy. On the other hand, Chapter 3 discusses the literature of federal government debt and federal government expenditure in Malaysia, the conventional and Islamic perspective of government debt, solutions to the problem of government debt, methods to evaluate government debt sustainability, and the conceptual framework of this thesis.

Chapter 4 outlines this thesis's research process. The chapter details on the research methodology, research design, conceptual framework, theoretical framework, research strategy, data collection, and data analysis techniques employed in this thesis. Meanwhile, Chapters 5, 6, and 7 are the analytical chapters. Chapter 5 is dedicated to fulfil RQ 1 and RQ 2 which relates to RO 1. Chapter 6 answers RQ 3 corresponding to RO 2. Chapter 7 addresses the final RQ and RO. Finally, Chapter 8 consolidates the findings from the analytical chapters, states the implications and limitations of this research, and provide suggestions for further research.

1.7   Conclusion

Chapter 1 provided an introductory discussion of this thesis. Background of the study, problem statement, ROs, RQs, significance of the study, and organisation of the study were presented.

Background of the study had centred on the use of *waqf* to finance Malaysian federal government public expenditure and how it will impact federal government debt. As such, ROs and RQs corresponding to the topic of this thesis were spelled out. The choice for this research was motivated by the rising federal government debt, persistent primary deficit, saturated literature on conventional debt economics, and lack of similar studies in the Islamic economics literature. This research is also of significance due to various reasons such as introducing the role of third sector in public finance and expounding the role of *waqf* outside of its typical religious purpose. There are a total of eight chapters in this thesis with two literature review chapters and three analytical chapters.

CHAPTER 2: WAQF: CONCEPT, SHARI'AH, AND PRACTICE IN SELECTED COUNTRIES

2.1   Introduction

This chapter exclusively reviews the literature on *waqf* and is organised as follows. Section 2.2 explains the concept and the *Shari'ah* of *waqf*. It is pivotal that the meaning and the *Shari'ah* of *waqf* are understood so that the thesis is rooted to its embodiment. In Section 2.3, the application of *waqf* in public finance is deliberated by exploring its historical and present applications. As this thesis generally stresses a place for *waqf* in public finance, literature on the application of *waqf* from past and present periods must be reviewed to provide detailed scrutiny of its evolvement. Review of the present *waqf* is done by examining *waqf* practices in several countries with advanced *waqf* implementation. Section 2.4 focuses on the literature of the Malaysian *waqf* setting in relevance to this thesis. The literature review is then synthesised to secure a place for public *waqf* in the Malaysian economy. Section 2.5 attempts to situate public *waqf* in the Malaysian economic setting. Lastly, Section 2.6 provides a brief conclusion to this chapter.

2.2   An Overview of *Waqf* and the Governing *Shari'ah*

Waqf is regarded as a pious endowment in Islam. From the literal perspective, *waqf* or its plural *awqaf* is defined as "hold, confinement or prohibition" (Kahf, n.d., p.2) while it technically means "holding certain property and preserving it for the confined benefit of certain philanthropy and prohibiting any use or disposition of it outside that specific objective" (Kahf, n.d., p.2). Thus, *waqf* is a voluntary or third sector component (Faridi, 1983; Kahf, 2014; Mohd Nahar & Mohamed Aslam, 2016) that is undertaken due to altruistic behaviour of humans and to attain Allah's pleasure. The voluntary sector "encompasses all such individual and social activities, which are not by intent or design,

undertaken to attain any economic or material benefit for the doer or doers, but generate wide ranging economic repercussions" (Faridi, 1983, p.35).

Indeed, *waqf* assists in poverty eradication, provision of pure and mixed public goods, education, health, as well as other related social services. This turns *waqf* into a religious object that can impact the economy. Due to this, Kahf (2014) defined *waqf* from the economic perspective as "diverting funds (and other resources) from consumption to investing them in productive assets which provide either usufruct or revenues for future consumption by individuals or group of individuals" (p.201). It must be stressed that the creation of *waqf* is strictly for benevolent causes that are permissible in Islam. Hence, *waqf* for pornographic dissemination, alcohol dealings, paying off *riba'* (usury), and other impermissible causes are absolutely abhorred.

Waqf is also called *boniyad* or *habs* in Iran and North Africa respectively (Çizakça, 1998), *vakf* in Turkish literature, and *wakaf* in most South East Asian literature. To avoid confusion, this thesis uses the term "*waqf*" or "*awqaf*" as they are widely used in the literature, unless stated otherwise in law enactments. There are unresolved claims that *waqf* originated from the civilisation of Mesopotamia, Rome, Greece, and pre-Islamic Arabs (Çizakça, 1998). However, the matter of origin is not a significant problem as the act of *waqf* is clearly founded in the tradition of Prophet Muhammad peace be upon him (PBUH). Unlike many other acts in Islam, the act of *waqf* was not sourced directly from the Quran (Çizakça, 1998; Babacan, 2011). The Quran, however, do contain verses regarding the act of giving which correlates with *waqf*. For instance, the Quran in Surah Ali Imran (chapter three) verse 92 states that, "By no means shall ye attain righteousness unless ye give (freely) of that which ye love; and whatever ye give, of a truth God knoweth it well".

The most prominent example of hadith that deliberated an act of *waqf* is given below:

Ibn Umar reported: Umar acquired a land at Khaibar. He came to Allah's Apostle (may peace be upon him) and sought his advice in regard to it. He said: Allah's Messenger, I have acquired land in Khaibar. I have never acquired property more valuable for me than this, so what do you command me to do with it? Thereupon he (Allah's Apostle) said: If you like, you may keep the corpus intact and give its produce as s*adaqa*. So 'Umar gave it as *sadaqa* declaring that property must not be sold or inherited or given away as gift. And Umar devoted it to the poor, to the nearest kin, and to the emancipation of slaves, aired in the way of Allah and guests.… (Sahih Muslim, Hadith 4006)

The hadith highlighted that the corpus of *waqf* must not be sold, inherited, nor given away freely. In other words, the corpus must remain intact as *waqf* and no ownership transfer is permitted. Another hadith classifies *waqf* as a continuous charity that is beneficial to Muslims even after death. It was narrated from Abu Hurairah that the Messenger of Allah PBUH said, "When a man dies, his acts come to an end, but three, recurring charity, or knowledge (by which people) benefit, or a pious son, who prays for him (for the deceased)" (Sahih Muslim, Hadith 4005). The term *sadaqah jariah* used in this hadith emphasises the permanence aspect of *waqf*.

2.2.1   The Principles of *Waqf*

Identifying the principles of *waqf* is important to ensure that the formulation and application of any *waqf* model adhere to the *Shari'ah*. Past studies often weighed more on the economic and financial impacts of *waqf* and lost sight of its spirit. As stated in Mohsin (2013), Al-Sarakhsi and Ahmad (1906) named three principles of *waqf* which are irrevocability, perpetuity, and inalienability. Similar principles were stated in Razali

(2015). These principles are also termed as key restrictions that the *waqf* becomes void if violated.

Irrevocability means a declared *waqf* asset will forever remain as *waqf* and cannot be revoked. Meanwhile, perpetuity stipulates that the corpus of *waqf* must remain permanently intact, non-perishable, and not cease easily. The Maliki madhab (Islamic school of law) however holds a different opinion in regards to these two principles. Maliki jurists opined that the ownership of *waqf* is reverted back to the founder when the usufruct from the corpus of *waqf* can no longer benefit the purpose of *waqf* in question (Layish, 1983). This case of temporary *waqf* was also argued to a large extent by Kahf (2014) in two facets; temporary *waqf* objective and temporary stipulations by *waqf* founder. The former enables the initiation of temporary *waqf* objectives such as caring of orphans until maturity, free private parking for a designated time, free journal subscription for a year, and others. On the other hand, the latter provides flexibility for the founder to revoke his or her *waqf* should s(he) falls severely ill, afflicted by natural disaster, or caught in any similar unusual circumstances that would require money.

One pertinent issue related to the perpetuity principle is the permissibility of cash, shares, unit trust, and other forms of financial rights to be endowed as *waqf*. This asset class that construes as movable properties, have volatile values due to inflation and trade. Hence, these assets are not legible for *waqf* endowment based on the perpetuity definition. However, people own more of this asset class as opposed to real estate properties, especially those from low and middle income class. Hence, their illegibility deters a large number of people from endowing *waqf*.

As mentioned in Mohsin (2013) and Çizakça (1998), Imam Zufar from the Hanafi madhab approves cash as *waqf* endowment. Meanwhile, the Shafi'e, Maliki, and Hanbali madhabs view assets eligible for *waqf* as everything with valid sales and can be renewed

occasionally by its usufruct or otherwise (Mohsin, 2009). In fact, Ebu's Su'ud, an Islamic jurist that had lived during the Ottoman ruling, is of the opinion that only contemporary custom shall or shall not limit the kind of asset suited for *waqf* endowment (Imber, 1997). Thus, cash, shares, unit trust, and other forms of financial rights that are the customary practices of today are legible for *waqf*. This is already acknowledged in certain *waqf* enactments. For instance, Section 23(1) of the Wakaf (State of Selangor) Enactment 2015 states that:

> The Corporation may accept—
>
> *(a)* shares, bonds, *sukuk* or other instruments for valuable guarantee; and
>
> *(b)* benefits from the units of share, bonds, *sukuk* or other instruments for the said valuable guarantee,
>
> given by way of *wakaf* by any person, society or institution provided that the business or investment carried out is consistent with Hukum Syarak.

Despite its flexibility, the *Shari'ah* (*Hukum Syarak*) must be uphold as obvious and written in the enactment.

Lastly, inalienability dictates that the corpus of *waqf* must not be sold, inherited, or given away as a gift. There is again flexibility in this principle through *ibdal* and *istibdal*. *Ibdal* means the actual selling of unproductive *waqf* property while *istibdal* is substituting the original *waqf* property with another *waqf* property by way of purchase (Department of *Awqaf*, Zakat and Hajj [JAWHAR], 2010a; Siraj, 2012). Although these two acts seem to violate the *waqf* principle, *ibdal* and *istibdal* are performed to present better alternatives to ensure perpetual benefit of *waqf*.

However, the four madhabs have different views regarding to these practices (JAWHAR, 2010b; Siraj, 2012). The Shafi'e and Maliki madhabs strictly forbid *ibdal*

12

and *istibdal* of immovable *waqf* property. Exclusions can be made in the Shafi'e madhab through order from the *Qadi* (judge). On the other hand, the Hanbali madhab holds a more open view as *ibdal* and *istibdal* of immovable *waqf* property can be done when a need arises or when there is benefit. The Hanafi madhab has almost the same view as the Hanbali in regards to immovable *waqf* property but differ in terms of *waqf* of mosque. *Waqf* of mosque can only go through *ibdal* and *istibdal* upon order form the Qadi. Even then, the generated return is used exclusively for another mosque. In terms of movable *waqf* properties, clear injunctions of it was found in the Maliki madhab where *ibdal* and *istibdal* of movable *waqf* property is permitted when a consensus is reached.

Different opinions attached to the principles prove the balanced view towards *waqf*. Although *waqf* in spirit is a religious tool, its flexibility stemming from the jurists' opinion make possible for *waqf* to also contribute outside of the religious norm. This includes the area of economics and finance. Aside from these three, there also exist other implied principles when a certain *waqf* is ambiguous. According to Kahf (2014), these are (1) *waqf* with no clear objective which signifies the *waqf* is for the poor, (2) when a *waqf*'s purpose becomes invalid, then that *waqf* becomes *waqf* for the poor and, (3) whenever a *waqf* deed is lost and its purpose becomes unknown, this particular *waqf* also becomes *waqf* for the poor. These side principles come naturally because the default of *waqf* creation is goodness and so shall it remain.

2.2.2 The Pillars of *Waqf*

The pillars of *waqf* guarantee clarity and complete fairness of the *waqf* endowment process. They also further ensure the validity of *waqf*. There are four pillars, namely the founder of *waqf* (*waqif*), the corpus of *waqf* (*mawquf*), the beneficiaries of *waqf* (*mawquf 'alaih*), and the statement of *waqf* (*sighah*) (Yayasan Waqaf Malaysia [YWM], n.d.a;

Mohsin, 2009; Razali, 2015). Mohsin (2009) added the fifth pillar namely the appointment of trustee (*mutawalli*).

In order for a person to be a valid *waqif*, (s)he must fulfil these conditions; a free person and the rightful owner of the asset intended for *waqf*, in full possession of his or her physical and mental faculties, *baligh* or have reached adulthood and, *waqf* is made voluntarily without any coercion. Thus, the first pillar safeguards the individual and the asset to be endowed from exploitation. Razali (2015) further clarified that it is also valid for government, non-Muslims, and any social bodies to endow *waqf*. The specific term for *waqf* endowed by the government is *waqf irsod* and the permissibility for non-Muslims to create *waqf* is in favour of Malaysia's multi religion setting. Permissibility of *waqf* creation by non-Muslims is based on the following hadith (Mohsin, 2009):

> Verily, Allah does not treat a believer unjustly in regard to his virtues. He would confer upon him (His blessing) in this world and would give him reward in the Hereafter. And as regards a non-believer, he would be made to taste the reward (of virtue in this world) what he has done for himself so much that when it would be the Hereafter, he would find no virtue for which he should be rewarded. (Sahih Muslim, Hadith 6739)

As for the pillar of *mawquf*, the following conditions must be fulfilled; benefits can be derived from that asset, the asset must have a price value, the asset must be completely owned by the founder, and the endowment is for noble purposes without violating any *Shari'ah* principles. This pillar actually assesses the suitability of an asset to continuously benefit as in the nature of *waqf*. In addition, Mohsin (2009) made it clear that the *mawquf* can be both movable and immovable properties.

Meanwhile, the beneficiaries of *waqf* can be Muslims, non-Muslims that obey the Muslim leaders, and free. The view that beneficiaries can consist of non-Muslims is based upon the action of Shafiyah binti Huyaii, the wife of Prophet Muhammad PBUH, whom had made her Jewish relatives as beneficiaries of *waqf*. As for those who do not fully possess his or her mental faculties and do not have a long life span such as prisoners in death row, they are not legible to become beneficiaries. The latter also includes situation like schools and orphanages that are about to close. The beneficiaries should also understand that receiving the benefits from *waqf* is to get closer to ALLAH. However, Mohsin (2009) put the rightful beneficiaries as those stated in the *waqfiyah* (*waqf* deed) which could be the *waqif*'s relatives, public individuals, or public charitable purposes. This is because the *waqif* should have a clear view to whom does his or her *waqf* is intended to. It protects the benefits of *waqf* from being channelled to the wrong recipients.

On the other hand, the *sighah* is valid whether it is pronounced explicitly or implicitly. Basically, *sighah* functions as a clear statement of a founder to create *waqf* endowment. In its written form, *sighah* is transcribed as a *waqf* deed to which Muslim jurists highly recommend (Mohsin, 2009). One advantage of *sighah* has already been alluded earlier, in which written *sighah* safeguards the rightful beneficiaries to receive the *waqf* benefit in question. Transcription of *waqf* deed also improves management efficiency and acts as an insurance in time of dispute. The final pillar in *waqif* is the designation of a *mutawalli* to manage the endowed *waqf* and a successor in case the existing *mutawalli* dies or incapable to carry out his or her duties. In fact, the *waqif* can also appoint himself or herself. Appointment of *mutawalli* is also crucial to ensure continuous operation of the *waqf* in question.

2.2.3   Ten Stipulations for *Waqf* Endowment and *Waqfiyah*

Waqfiyah documents detail on *waqf* endowment such as the purpose of *waqf*, rightful beneficiaries, and manner of administration. The administration matter directly correlates with the ten stipulations or five pairs of stipulations for *waqf* endowment. Claimed by Abu Zuhrah (1972) in Mohsin (2009), the stipulations originated from the Hanafi madhab which had named the five pairs as *ziyadah* (increase) and *nuqsan* (decrease), *idkal* (addition) and *ikhraj* (removal), *i'ta'* (granting) and *hirman* (dispossession), *taghyir* (replacement) and *tabdil* (conversion), as well as *istibdal* (substitution) and *ibdal* (exchange). These five pairs of stipulations are also accepted by the remaining three madhabs (Mohsin, 2009).

Ziyadah and *nuqsan* give flexibility to the founder to prioritise between various groups of rightful beneficiaries. Assume that the revenue from any *waqf* created was to benefit a mosque and orphanage equally. However, the *waqif* or *mutawalli* soon realise that the orphanage is in direr need of the revenue than the mosque. Thus, the *mutawalli* can increase the contribution to the orphanage by up to say 65 percent of the revenue and decrease the share of the mosque to 35 percent. Meanwhile, *idkal* and *ikhraj* give room to the *waqif* or *mutawalli* to include another beneficiary that has more need of *waqf* and exclude another existing beneficiary that no longer requires it. An example can be given as such. Revenue stream from this theoretical *waqf* is to be used to build a public park. When finished, the *waqif* or *mutawalli* can remove the public park as a beneficiary and add scholarships for students since they are more in need of it.

On the other hand, *i'ta'* and *hirman* allow the *waqif* or *mutawalli* to give away all or a portion of *waqf* revenue to whoever s(he) wills for a period of time and dispossess whoever s(he) wills. For instance, the *waqif* or *mutawalli* can choose to give away all or a portion of the revenue from a specific *waqf* that was initially meant for a school to an

orphanage that needs the benefit more. As for *taghyir*, it gives the right for *waqif* to replace the use of *waqf* revenue with another while *tabdil* gives the right to completely change the *corpus* itself. Example of *taghyir* is replacing the use of revenue stream from property repairs to financing new poor students in case of a school. Example of *tabdil* can be showcased as the following. A *waqif* initially creates a *waqf* of agricultural land but the land becomes barren after a few years. Therefore, the *waqif* or *mutawalli* has the right to change the land's purpose and build a business complex instead. Lastly, *ibdal* and *istibdal* were already defined and explained in Section 2.2.1.

It must be made clear that the first four pairs of stipulations can only be carried out when the *waqif* states them in the *waqf* deed (Mohsin, 2009). As has been discussed earlier, these four stipulations do not at all intent to change the nature of *waqf*. In fact, they can be viewed as methods to ensure that revenue or benefits from *waqf* continue in perpetuity and its very basic precept of goodness is thoroughly embodied. The last two stipulations also share similar motive. Hence it is crucial that new *waqif* is informed of these ten stipulations and encourage them to write these stipulations, especially the first eight. If not, the *waqf* could be deemed as ambiguous and subjected to the implied principles outlined by Kahf (2014) that was discussed towards the end of Section 2.2.1.

2.2.4 Classification of *Waqf*

The purpose for endowing *waqf* are vast. Due to this fact, studies had categorised *waqf* according to its general purposes. Kahf (2014) and Mohammed Obaidullah (2008) categorises *waqf* into religious, philanthropic, and private purposes. Examples of religious *waqf* are for building mosques and cemetery upkeep, while examples of philanthropic *waqf* are provision of public goods and mixed public goods, environmental and animal care, as well as other social services. Lastly, private *waqf* are for the benefits

of the *waqif*'s descendants. Meanwhile, Bonine (1987) and Babacan (2011) divided *waqf* into public or charitable *waqf* and private or family *waqf*. The former is founded to provide for social needs and economic services, while the latter is for the benefit of the founder's lineage. Mohsin (2009) classified *waqf* into three. The first is *waqf khayri*, the second is *al-waqf al-dhurri, al-waqf al-ahli,* or *waqf 'ala'-wlad*, and the third is al-*waqf al-mushtarak*. The first and second classifications of *waqf* respectively bear the same meaning as public *waqf* and private *waqf*. Meanwhile, the third classification is simply the hybrid of the first two classifications.

There are also other categorisations of *waqf* according to its specific purpose. Mohamad Akram, Mek Wok, and Mohd. Fuad (2008) as well as Siti Mashitoh (2014) divided *waqf* into *'am*, *khas*, and *al-mushtarak*. *Waqf 'am* are founded for the purpose of providing social needs and economic services in general without stating any specific purposes while *waqf khas* specifies the purpose. These definitions are similarly stated as *wakaf am* and *wakaf khas* in Wakaf (State of Selangor) Enactment 2015, Wakaf (State of Malacca) Enactment 2005, Wakaf (Negeri Sembilan) Enactment 2005, and Wakaf (Perak) Enactment 2015. Meanwhile, hybrid *waqf* or *wakaf musytarak* is simply a mix of different classifications of *waqf* as mentioned in Johor Wakaf Rules.

It is noticed that the categorisation of *waqf 'am* is not based on specified beneficiaries. This seemingly contradicts with the definition of *waqf* given by Kahf (n.d.) whereby the objective of *waqf* should be specifically stated. Instead, it actually follows the stipulation of *idkal* and *ikhraj*. The reality is, the concept and the governing *Shari'ah* of *waqf* are largely based on *ijtihad* (Mohamad Akram et al., 2008; Kahf, 2014). *Ijtihad* is a process where Islamic jurists cohesively agree on the solution to a legal question. From *ijtihad*, many opinions emerged with regards to the many flexibilities of *waqf* that were discussed in the earlier sections.

2.3   The Application of *Waqf* in the Economy and Public Finance

The *ijtihad* process and the nature of *waqf* extends the use of *waqf* outside the religious sphere and into the economic sphere, forming the categories of public *waqf*, philanthropic *waqf*, and *waqf 'am*. The most striking *waqf* application that is directly related to the topic of this thesis is in the public finance section. Specifically, public goods, mixed public goods, and other social services were provided by *waqf* in Islamic history. In fact, the *waqf* application was enormously significant towards the economy back then.

Çizakça (1998) firmly believed that these very principles of *waqf* makes it a suitable tool to finance pure and mixed public goods that are often catered by government expenditures, "The importance of the waqf system lies precisely here; for it is the very institution which transforms alms into a myriad of services in perpetuity (p.47). The principle of irrevocability deters mismanagement of *waqf*, inalienability constraints *waqf* for the use of pure and mixed public goods only, while perpetuity ensures consistent delivery of pure and mixed public goods. In fact, the benefits of *waqf* extends beyond the notion, "… assuming that the efficiency problems are solved, the *waqf* system can significantly contribute towards that ultimate goal of every modern economist; massive reduction in government expenditure, which leads to a reduction in the budget deficit, which lowers the need for government borrowing …" (Çizakça, 1998, p.44)

2.3.1   *Waqf* in Public Finance of the Past

The literature claimed that *waqf* is one of several sources of revenue for early Muslim governments which was specifically used to finance pure and mixed public goods as well as other social goods and services (Faridi, 1983; Siddiqi, 1995; Gil, 1998; Babacan, 2011;

Kahf, 2014). Public goods are "goods that are non-excludable (not easily denied to unauthorised consumers) as well as non-rival (capable of being enjoyed by many consumers at once)" (Kuran, 2001, p.841). Examples of public goods include but not limited to national defence, public transportations, and clean environment. Meanwhile, mixed public goods are goods that have both the characteristics of private and public goods. In the Islamic context, mixed public goods also constitute public goods (Akhthar, 1995).

Kahf (2014) and Gil (1998) mentioned several public goods that were converted into *awqaf* by exemplary Islamic figures; Prophet Muhammad PBUH had used properties that was left by Mukhayriq as *waqf* to finance for defence, and Uthman bin Affan had bought a well in Madinah to provide free drinking water for all Muslims. These two cases of *awqaf* occurred after Prophet Muhammad PBUH migrated to Madinah which soon became the first Islamic state (Gil, 1998). Madinah was a relatively small state which one may argue the obvious relevance of *waqf* for the provision of public goods back then.

On the contrary, the number of *waqf* property proliferated such that Diwan al-Ahbas was formed during the Umayyad Caliphate at the state level to avoid misuse of *waqf* (Mohsin, 2009). From this point on, the *Shari'ah* court is responsible to supervise all *awqaf* in the Muslim state while the founders are responsible for the management of *waqf* that s(he) created. In this era, *awqaf* for education were highly demanded and mushroomed, including libraries, schools, financing teachers, as well as sponsorship of scholars and students (Mohsin, 2009). This was perhaps the earliest form of *waqf* for mixed public goods.

The purpose of *waqf* further expanded to include other social services during the Abbasid reign (Kahf, 2014). Universities in Damascus had given money allowances, servants, medical care, and other services to students while simultaneously provided *waqf*

for road maintenance, *waqf* for the poor to go to Hajj, as well as *waqf* for getting married. A *waqf* investment fund comprising of business, residential rental buildings, and agricultural lands was also set up to finance hospital operating expenses. It is interesting to point out that business is regarded as a riskier investment than real estate which could jeopardise the return on investment. Instead, the said *waqf* investment fund remarkably resembles Portfolio Theory whereby risk can be minimised and return optimised by holding a diversified portfolio of assets with different risk levels (Brealey, Myers & Allen, 2011).

Sultan Salahuddin al Aiyyubi of the Ayyubid dynasty introduced a new *waqf* policy in the Nile Valley (Frenkel, 1999) by systematically converted bounties from war into *awqaf* and endowing *awqaf* himself. A proliferation of *awqaf* resulted from this policy such as schools, hospitals, shops, food, public bath, water supply, defence, housing, and several others. The sultan had also ordered old *awqaf* to support new *awqaf*. This further cemented the idea that *waqf* can finance both the public and mixed public goods, as well as other social services.

A passing look at Sultan Salahuddin al Aiyyubi's *waqf* policy shows the transition of *waqf* into the public sector. This was even more evident during the Ottoman Caliphate. Babacan (2011) went as far to claim that *waqf* was a third fiscal category alongside the *timar* system and state treasury. *Waqf* had financed schools, supported retired sailors, payed for commuter ships, defended town, provided water supply, paid tax for fellow countrymen, created employment opportunities, and many others (Peri, 1992; Çizakça, 1998; Babacan, 2011). The Ottoman Caliphate had brought further progress to the *waqf* system by approving the use of cash *waqf* to finance the building of mosque, soup kitchen, school, and several others (Mandaville, 1979).

In addition, the Sultan Salahuddin al Aiyubi's *waqf* policy states that *waqf* is an instrument of the public sector. This is because the *mawquf* had earlier became the state's possession or revenue. However, in the case of the Ottoman's, not all *mawquf* was sourced from the state revenue. Some are sourced from the wealthy (Kuran, 2001), hence do not make *waqf* an instrument solely from the public sector but also from the third sector. As such, claiming *waqf* as a third fiscal category in the Ottoman Rule is not quite correct. In addition, although *waqf* did finance items of modern public expenditure in the past, the literature did not provide sufficient evidence that *waqf* can directly finance public expenditures. It is a literature gap that directly correlates with the first RO of this thesis.

The *waqf* system started to show signs of degradation in the early nineteenth century due to a number of reasons. The first reason is the use of *istiqlal* to derive income by lending out cash *waqf*. *Istiqlal* is a form of sales contract at which the borrower sells his real estate to the lender and the lender rents out that particular real estate to the borrower within the period of debt; with the rental almost always ten percent of the loan (Çizakça, 1998). Therefore, *istiqlal* actually allows the cash *waqf* to gain income by converting it into an interest bearing loan which is abhorred in Islam (Mandaville, 1979; Çizakça, 1998). The only reason that *istiqlal* was accepted in the Ottoman Caliphate was because this instrument is seen as a customary practice (Mandaville, 1979). Secondly, the practice of cash *waqf* had ignored the aspect of capital accumulation (Mandaville, 1979; Çizakça, 1998). Çizakça (1998) assumed more income could be gained and loss could be avoided if the cash *waqf* were given to finance businesses instead of merely for consumption. In other words, Çizakça (1998) proposed investment for cash *waqf*.

Centralisation of *waqf* by the Ottoman state in the middle of the 19th century had also contributed to the demise. Çizakça (n.d.) was of the opinion that the centralisation had brought about two consequences. Firstly, the bureaucratic procedures to create *waqf*

became more complicated and deterred further establishment of *awqaf*. Secondly, the centralisation permitted the Ottoman government to indulge in corruption. One example given by Çizakça (n.d.) was the force on the *waqf* system to participate in economic ventures with high probability of loss.

On the contrary, Peri (1992) claimed that corruption was the very reason that the Ottoman state decided to centralise *waqf* on the first place. Corruption had long festered in the Ottoman's *waqf* system. An instance is the case of public *awqaf* at Damascus and Jerusalem between the sixteenth and the twentieth century. Baer (1997) argued that the founder of those public *waqf* would usually appoint a family member to manage the system which furthered the family's personal interest. Baer (1997) supported this assertion by claiming that administrators of *waqf* received large portion from the *waqf* income and left the beneficiaries with less. On top of that, the administrators of these public *awqaf* are influential people who sometimes caused certain social and political ramifications; a similar situation to when a tycoon with ill intention funds an election campaign. Baer (1997) believed that these administrators only wanted to gain control of the public goods. Thus, it is fair to say that corruption is an isolated problem while bureaucracy remains.

Peri (1992) and Babacan (2011) argued that corruption was actually due to vaguely defined *waqf* deed. In studying the poor kitchen of Hasseki Sultan in Jerusalem, Peri (1992) found that the beneficiaries also included well-to-do individuals instead of the poor; a clear consequence of manipulation of the *waqf* deed. Catering both well-to-do individuals and the poor had greatly increased the expenses of *waqf*. Since this practice had spread all over the Ottoman Empire, the *waqf* system became burdened with excessive debt and soon collapsed (Peri, 1992). This here lies the importance of documenting a clear *waqf* deed. Lastly, *waqf* had also collapsed because of the inability

of its past practice to assimilate into a rapidly industrialising economy, "the historical pattern might have been different had the regulations governing the waqf evolved into an enterprise enjoying corporate status" (Kuran, 2001, p.843).

The quoted phrase by Kuran (2001) injects optimism that *waqf* can be momentous in this current economy. Apart from instituting *waqf* as described by Kuran (2001), the present Islamic world should also address the issues of corruption, bureaucracy, vaguely defined *waqf* deed, and how to increase *waqf* capital. These are also the issues that should be address to fulfil RO 2 of this thesis. With the advancement of Islamic economics and Islamic finance, these mentioned shortcomings can surely be tackled. The next section starts the discussion of *waqf* in the present economic setting.

2.3.2   *Waqf* in Public Finance of the Present

In contrary to past practice, the present *waqf* application in public finance is not as significant. *Waqf* in this modern economy is no longer the major provider of pure and mixed public goods as well as related social services. Instead, the role is fulfilled by the government. It is however bias to state that the Islamic world has not taken any strides in realising *waqf*'s true potential. *Waqf* possesses evolutionary characteristics that makes it a practical instrument for any era (Adi, 2014), hence every issues concerning *waqf* was tackled to a certain extent.

For one, corporate *waqf* is gaining traction in the modern era. It is defined as "the confinement of an amount of liquid money, shares, profits, dividends by founder(s) such as individuals, companies, corporations, organizations, or institutions, and the dedication of its usufruct in perpetuity to the welfare of society" (Mohsin, 2014, p.16). A *waqf* corporation is responsible to perform the tasks assigned by *waqif* especially in managing

and investing *waqf* funds. It also has limited liability and comprises a board of directors. In what follows, a few countries that are viewed as having good *waqf* practice are discussed in order to grasp a general idea on the role of *waqf* in modern public finance.

2.3.2.1 *Waqf* in Kuwait

Sait and Lim (2006) named Kuwait as "the leader in *waqf* management, is worthy of especial notice in demonstrating the kinds of innovation that can assist the institution to make progress" (p.166). *Waqf* in Kuwait is presently managed by the Kuwait Awqaf Public Foundation (KAPF), an independent governmental organisation under the aegis of the Minister of Awqaf and Islamic Affairs (Busharah, 2012). KAPF is responsible to encourage and manage *waqf* endowments as well as coordinating with government and non-government bodies in carrying out projects that coincide with the conditions set by *waqif* (Busharah, 2012). Management of *waqf* endowments include investing *waqf* assets and taking care of other *waqf* affairs. In fact, KAPF was tasked by the Organisation of Islamic Cooperation (OIC) to coordinate *waqf* actions among Muslim countries (KAPF, n.d.a.; Kuwait News Agency, 1999).

KAPF has created a sustainable investment policy of *waqf* which inadvertently addresses the issue of capital accumulation identified in the previous section. Its policy aims for a risk free investment of *waqf* asset with gradual increases in revenue (Busharah, 2012). Its investment strategy requires the fulfilment of these criteria; economic, *Shari'ah*, diverse geographic, diversified investment instruments, multiple investment sectors, and regulations (Busharah, 2012). The economic criteria necessitate the conduct of feasibility studies for every investment activity while the *Shari'ah* criteria take into account the factors to minimise the risk to safeguard the *waqf* capital. Diversifying

geographic, investment instruments, and sectors entails investments in separate locations, different investment portfolios, and various sectors such as real estate, services and such.

It is also not entirely wrong to assume that the business model of KAPF is that of a corporate *waqf* based on three reasons. Firstly, KAPF has a board of directors known as the Awqaf Affairs Council consisting of the Minister of Awqaf and Islamic Affairs as the President, six members, and three experts (KAPF, n.d.b). The members are the Awqaf Secretary General, Deputy of the Ministry of Awqaf and Islamic Affairs, the Director-General of the Social Insurance Institutions, the Director-General of Zakat House, Finance Ministry representative, and Body-General Representative for Investment. Meanwhile, three experts are nominated based on a three-year renewable term. Secondly, KAPF invests *waqf* funds based on an outlined *waqf* investment policy. Thirdly, KAPF also publishes annual reports like most corporations. Publication of annual reports indirectly ensures the transparency of KAPF's operation and reduces corruption.

It is relatively difficult to state about bureaucracy of *waqf* management in KAPF, especially the way *waqf* deed is articulated in Kuwait. One thing that is certain is that a person can easily become *waqif* and endow *waqf* via an online platform (KAPF, n.d.c). Busharah (2012) added that *waqf* shares offered by KAPF is cheap and provides opportunity for middle class income earners to endow *waqf*. On top of that, KAPF also organises outreaching program of potential *waqif* (Busharah, 2012). Outreach program and online *waqf* endowments greatly facilitate the persons to endow *waqf* and simultaneously reduces bureaucracy.

In regards to public finance, it is observed that KAPF can almost rival the provision of public goods and other social services by *awqaf* in Islamic history. Ten *waqf* funds have been established which are for disabled individuals, mosques upkeep, health development, family care, science development, preserving the environment, Quran and

its teaching, culture and thought literature, community development, and Islamic countries and community cooperation (Busharah, 2012). Still, more funds can be added when other society need arises. Interestingly, these *awqaf* funds have board of directors that partially consist of members from the public which show a combination of public and private sectors management.

2.3.2.2 *Waqf* in Egypt

It is pertinent to discuss about Egyptian *waqf* because the country possesses one of the oldest *waqf* recorded in history, the Al-Azhar University. In addition, Egypt was once under the Ottoman rule, an era where *waqf* had reached its pinnacle. Thus, if one wants to trace the evolution of *waqf* in modern economics, Egypt is the country to study.

The Egyptian Awqaf Authority (EAA), an independent body that reports to the Ministry of *Awqaf*, is responsible for managing and investing *waqf* in order to generate maximum revenue (Bakhoum, 2014). The EAA are managers of all *awqaf* in Egypt except for (Bakhoum, 2014. p.15):

a) Agricultural lands that are endowed for public charity and became under the General Authority for Agrarian Reform according to law 152 / year 1957.

b) Agricultural lands that are endowed for private charity and became under the General Authority for Agrarian Reform according to law 44 / year 1962.

c) Charitable endowments where the endower stipulates that he and his descendants supervise them.

d) The *awqaf* that are being supervised under the Coptic Orthodox Awqaf Authority

e) The money of exchange (*badal*) or *hikr*

f) Bonds of agrarian reform, their value of what was used from them and their revenue

g) The *awqaf* that are supervised by the Ministry of Awqaf

The EAA also adopts the corporate *waqf* model. It has board of directors and generates *waqf* revenue by investing *waqf* funds in agriculture, housing, banks, insurance, and other industries (Khalil, Ali, & Shaiban, 2014). Egyptian *waqf* revenues are allocated for maintenance of *awqaf* assets, investment and development of *awqaf* resources, technical matters, beneficiaries, and others such as healthcare and education (Khalil et al., 2014). To the knowledge of this researcher, there is no reference on who the beneficiaries are. Taking only education and healthcare into account, the *waqf* system in modern Egypt pales to the *waqf* system in Islamic history in terms of public finance. Compared to Kuwait, Khalil et al. (2014) claimed that Egypt's *waqf* revenue is not as profitable which is unavoidable because of Egypt's economic and political turmoil.

Even though Egypt's *waqf* system towards public finance could not rival the past, there are attempts for improvement. During the rule of Hosni Mubarak (1981 – 2011), the Ministry of *Awqaf* had introduced a new strategy called *majhud dhati* or *juhud dhatiyya* meaning "self-effort" to encourage mosque to become welfare providers and provide services such as teaching mathematics to computer science, healthcare, professional trainings, kindergartens, and others (Pioppi, 2004). In other words, the Egyptian government pushed the Egyptian society to "autonomously find the economic resources to finance those services and support activities that used to be a state duty" (Pioppi, 2004, p.5). This strategy is almost similar to what this thesis is attempting to propose, argue, and defend. It depicts an ideal Islamic economy described by Faridi (1983) where the private and third sectors play a much larger role in the economy than the public sector.

However, it is almost impossible to firmly state the progress of *majhud dhati* due to the scarce literature. On top of that, there is the morale dilemma of completely leaving the welfare of the society to private and third sector initiatives. Regardless, Bakhoum (2014) claimed that EAA and the Ministry of *Awqaf* do not have a clear set of system, procedures, and maintenance guidelines for their *awqaf* properties thus insinuating that Egyptian *awqaf* are still managed by the government. As such, the literature gap on the practicality of *waqf* to finance public expenditure remains an open question.

2.3.2.3 *Waqf* in Singapore

Waqf system in Singapore is deemed as one of the most comprehensive and efficient *waqf* management in South East Asia. According to the Administration of Muslim Law Act (AMLA) in 1968, all *awqaf* created in Singapore are vested under Majlis Ugama Islam Singapura (MUIS) or the Islamic Religious Council of Singapore (Shamsiah, n.d.). Due to inefficient management and cases of *waqf* property being sold, the AMLA was amended in 1995 and required all *awqaf* properties to be registered with MUIS. Later on, MUIS formed a wholly owned subsidiary of a corporate entity, Warees Investments Pte Ltd in 2000 to increase efficiency.

The *waqf* management in Singapore systematically and fiercely addresses most of the issues identified in Section 2.3.1. Firstly, MUIS instituted a wholly owned subsidiary which is the Warees Investments Pte Ltd to assist the management and administration of *awqaf* that is increasingly complex. Secondly, Singapore's *awqaf* accumulate capital through innovative means which are internal Real Estate Islamic Trust (REITs), *sukuk* (Islamic bond), and deposit cash *waqf* scheme (Shamsiah, n.d.). In internal REITs, *waqf* properties with low yield acquire a piece of a high yield property by buying shares of said property to obtain income. *Sukuk* instrument was undertaken to borrow large sums of

funds for projects in prime location, while compulsory cash *waqf* scheme entails compulsory contribution of cash by Muslim employees.

Thirdly, MUIS tackles the issues of corruption seriously. Aside from requiring all *awqaf* in Singapore to be registered, these *awqaf* are also subjected to auditing (Shamsiah, n.d.) thus garnering positive impression on potential *waqif*. In addition, MUIS has successfully developed a complete *awqaf* accounts and *waqf* database management system (Shamsiah, n.d.). With this system, it is easier for MUIS to channel *awqaf* proceeds to the rightful beneficiaries as stated in the *awqaf* deeds. The ease of allocating proceeds to beneficiaries suggests that the *awqaf* deeds are well articulated. Fourthly, Mohsin (2013) explained that Singaporean Muslims can opt for *waqf* deduction based on their monthly gross income through an automatic check off system. This is indicative of an easy *waqf* endowment procedure. With this, all of the points indicate that Singapore adopts a corporate *waqf* model. In terms of public finance, goods and services that are provided by the *waqf* system in Singapore are mosques, madrasah (religious schools), education, and social welfare (Shamsiah, n.d.). Hence, the *waqf* system in Singapore is in parallel to the *waqf* system in Islamic history in terms of pure and mixed public goods provision.

Although the *waqf* system in these countries from the public finance perspective are not as significant as the past, certain advancements still occurred. The governance of *waqf* in these three countries are impressive, especially in Kuwait and Singapore. The issues of transparency, bureaucracy, and *waqf* financing were tackled and corporate *waqf* was successfully instituted. Still, are these the only issues that *waqf* financing public expenditure will face in the context of modern economy? On top of that, do these issues relate to Malaysia in the first place? If they do, are the solutions to the identified issues the same for Malaysia or different strategies are needed? It is thus essential to acquire an

understanding of *waqf* in Malaysia. The next section offers a comprehensive review on this matter.

2.4   The *Waqf* Practice in Malaysia

As is evident from the Ninth Malaysia Plan, the Malaysian federal government has been striving to improve the *waqf* institution. As a result, there is a rise of *waqf* in terms of social services, education, healthcare, and economics. The employment of cash *waqf* opened the opportunity for middle income class and possibly lower to endow *waqf*. Corporate *waqf* was also established and forms an essential entity that can bring forward Malaysian *waqf* in this modern economic setting. However, as we shall see, there are still ongoing issues that have to be addressed.

2.4.1   The Legal Framework of Malaysian *Waqf*

Western imperialism had segregated religion from economics, finance, law and order, and other segments prior to the Malaysian independence. As a result, there was none if not little *waqf* for education, healthcare, or any similar social services for that matter. What remains was mostly only *awqaf* for cemeteries and mosques (Çizakça, 2000). After independence, the Federal Constitution was enacted and almost all *waqf* related matters were transferred under the ruler and state jurisdiction. As contained in Item 1 of the Ninth Schedule under List Two-State List of the Federal Constitution (p.198):

Except with respect to the Federal territories of Kuala Lumpur, Labuan and Putrajaya, Islamic law and personal and family law of persons professing the religion of Islam, including the Islamic law relating to succession, testate and intestate, betrothal, marriage, divorce, dower, maintenance, adoption,

31

legitimacy, guardianship, gifts, partitions and non-charitable trusts; Wakafs and the definition and regulation of charitable and religious trusts, the appointment of trustees and the incorporation of persons in respect of Islamic religious and charitable endowments, institutions, trusts, charities and charitable institutions operating wholly within the State; Malay customs; Zakat, Fitrah and Baitulmal or similar Islamic religious revenue; mosques or any Islamic public place of worship, creation and punishment of offences by persons professing the religion of Islam against precepts of that religion, except in regard to matters included in the Federal List; the constitution, organization and procedure of Syariah courts, which shall have jurisdiction only over persons professing the religion of Islam and in respect only of any of the matters included in this paragraph, but shall not have jurisdiction in respect of offences except in so far as conferred by federal law; the control of propagating doctrines and beliefs among persons professing the religion of Islam; the determination of matters of Islamic law and doctrine and Malay custom.

According to the above, *waqf* is under the jurisdiction of Malaysian States authorities which are either the Sultan, Yang di-Pertuan Agong, or Yang di-Pertua Negeri. In turn, the Ruler of Malaysian States and Federal Territories appoint the SIRCs to be the sole trustees of *waqf* in Malaysia which is stipulated in all states' statutes (Siti Mashitoh, 2011). However, Çizakça (2000) heavily criticised this law as it abandons the traditional way of letting *waqif* appoints the trustees.

In turn, the Malaysian States can enact their own *waqf* laws subjected to certain restrictions. This is according to Article 74 of the Federal Constitution which must be read together with the State List of the Ninth Schedule (Siti Mashitoh, 2011). Article 74(2) and Article 74(3) of the Federal Constitution state that (p.72):

(2) Without prejudice to any power to make laws conferred on it by any other Article, the Legislature of a State may make laws with respect to any of the matters enumerated in the State List (that is to say, the Second List set out in the Ninth Schedule) or the Concurrent List.

(3) The power to make laws conferred by this Article is exercisable subject to any conditions or restrictions imposed with respect to any particular matter by this Constitution.

Similar condition applies to Federal Territories in accordance to Item 4(k) and Item 6(e) of the Ninth Schedule List I-Federal List (Siti Mashitoh, 2011).

4. Civil and criminal law and procedure and the administration of justice, including –

(k) Ascertainment of Islamic law and other personal laws for purposes of federal law

6. The machinery of government, subject to the State List, but including –
(e) Government and administration of the Federal Territories of Kuala Lumpur, Labuan and Putrajaya including Islamic law therein to the same extent as provided in item 1 in the State List and in respect of the Federal Territory of Labuan, native law and custom to the same extent as provided in item 13 of the Supplement to State List for States of Sabah and Sarawak;

Since each state has the power to enact their own *waqf* laws, the *waqf* laws in Malaysia vary from one state to another. This has caused much complexity in the development of *waqf*, including one question of whether the difference between state *waqf* laws affect *waqf* for financing public expenditure. This question presents a gap that this thesis has to fill.

In regards to this, there were studies conducted to instate uniform *waqf* laws in Malaysia (Sharifah Zubaidah & Nor Asiah, 2014; Sharifah Zubaidah, 2016). It is believed that a standardised *waqf* law can stimulate cheaper transaction costs, enhance transparency, inculcate positive public perception, and lessen bureaucracy (Sharifah Zubaidah & Nor Asiah, 2014; Sharifah Zubaidah, 2016). The federal government is also in support of this idea. JAWHAR produced the *Manual Pengurusan Model Perundangan Wakaf* (Manual of *Wakaf* Legislation Model Management) with the hopes that Malaysian states will copy the manual and thus streamline the laws of *waqf* in Malaysia. This effort was however unfruitful as only Perak strictly followed the said manual (Sharifah Zubaidah, 2016).

Another suggestion is to instate Federal Territories *Waqf* Act that can serve as a model law through negotiations with Malaysian states (Sharifah Zubaidah, 2016). Should this act materialise, Article 75 of the Federal Constitution which states, "If any State law is inconsistent with a federal law, the federal law shall prevail and the State law shall, to the extent of the inconsistency, be void" can take effect and thus *waqf* laws will become uniformed. However, despite more than a decade of negotiation efforts, the act has never been passed (Sharifah Zubaidah, 2016) mainly due to sensitivities regarding the State Laws and the jurisdiction of Rulers within each state. This is unlike that of Islamic Banking Act (IBA) 1983. Markom, Pitchay, Zainol, Rahim and Merican (2013) alluded that IBA (1983) was successfully instituted because banking falls under Items 7 and 8 of the Federal List in the Federal Constitution.

Nonetheless, there are SIRCs that realise the dire need for proactive *waqf* laws. These are the states of Johor, Melaka, Negeri Sembilan, Selangor, and Perak (Sharifah Zubaidah, 2016). These SIRCs introduced the Wakaf (State of Malacca) Enactment 2005, Wakaf (State of Negeri Sembilan) Enactment 2005, Wakaf (State of Selangor) Enactment

2015, and Wakaf (State of Perak) Enactment 2015. On the other hand, Johor has long instituted its detailed *waqf* procedure through Johor *Wakaf* Rules. Although most of the states do not strictly follow the Manual of *Wakaf* Legislation Model Management, the amendments made are progressive in nature. Three such amendments are allowing other entities to manage *waqf*, cash *waqf* scheme, and *waqf* of shares.

The stipulations that allow other entities to manage *waqf* are Section 27(2) of Wakaf (State of Perak) Enactment 2015, Section 33(1) of Wakaf (State of Negeri Sembilan) Enactment 2005, and Section 4(1) of Wakaf (State of Selangor) Enactment 2015. Assigning and permitting others to be *waqf* managers increase the freedom of creating and managing *waqf* using personalised procedures within *Shari'ah* purview. Inadvertently, *waqf* should be able to rise. More discussions on private *waqf* managers or *nazir khas* are included in Section 2.4.2

Meanwhile, the use of cash *waqf* scheme is detailed in Section 21 and Section 22 of Wakaf (State of Selangor) Enactment 2015, Section 17 of Wakaf (State of Malacca) Enactment 2005, Section 11 of Wakaf (State of Negeri Sembilan) Enactment 2005, Section 13 (2) of Johor Wakaf Rules, and Section 11 and 34 of Wakaf (State of Perak) Enactment 2015. Cash *waqf* is defined as endowing cash as *waqf* to any trustee of which the capital is reserved for the beneficiaries (JAWHAR, 2010a). It is important to note that *waqf* shares is a variant of cash *waqf* because *waqf* shares is bought with cash and it is that cash which is being endowed to the SIRC. Section 2 of Wakaf (State of Malacca) Enactment 2005 defines *waqf* shares as the creation of *waqf* through the issuance of shares which are subsequently endowed as *waqf* by the buyer to the SIRC. The permissibility of cash *waqf* in Malaysia stems from a fatwa by the National Fatwa Council Islamic Affairs of Malaysia that convened on 10th to 12th April 2007. Through cash *waqf* scheme and *waqf* shares, *mawquf* are no more restricted to real estate, thus open the doors for more

types of *waqf* endowments. As a result, even middle income class and possibly lower class individuals can be a *waqif*. In fact, *waqf* shares and cash *waqf* are entitled for tax exemption as stated in Section 44(6) of the 1967 Income Tax Act.

Lastly *waqf* of shares is accepted due to Section 23 of Wakaf (State of Selangor) Enactment 2015 and Section 13 (1) of Johor Wakaf Rules. *Waqf* of shares is shares of firms or the firms' existing shares committed for *waqf* (Siti Mashitoh, 2011). An indirect effect of this is the creation of corporate *waqf*, "the confinement of an amount of liquid money, shares, profit, dividends by founder(s) such as individuals, companies, corporations, organizations or institutions, and the dedication of its usufruct in perpetuity to the welfare of society (Mohsin, 2014, p.16)". Johor Corporation (JCORP) is an excellent example of a corporation that employs corporate *waqf*.

The resulting effect of these proactive laws are significant in terms of *waqf* development. SIRC of Selangor for instance, had appointed Urus Maju Ehsan Sdn. Bhd. to develop *awqaf* lands in Selangor (Urus Maju Ehsan, n.d.) and SIRC of Negeri Sembilan had given consent to Islamic Science University of Malaysia (USIM) to establish the university's own education *waqf* fund named Al-Abrar Waqf Fund (Center for Awqaf and Zakat, n.d.a). Separate institutions to handle *waqf* matters was also established such as Perbadanan Wakaf Negeri Sembilan (PWNS) created by the SIRC of Negeri Sembilan and Perbadanan Wakaf Selangor (PWS) created by SIRC of Selangor. PWS had also formed partnership with Bank Muamalat Malaysia Berhad (BMMB) to jointly manage a *waqf* fund called Wakaf Selangor Muamalat (WSM) (WSM, n.d.a). On top of that, JCORP has endowed a sizable sum of listed and unlisted company shares as *waqf* (Abd. Shakor, 2011). These *waqf* of shares are managed and trusted to Waqaf An-Nur Corporation Berhad (WANCORP) which was appointed by JCORP and recognised by the SIRC of Johor as a *nazir khas* of *waqf*. Of recent, WANCORP has also been appointed

as the *nazir khas* for Larkin Sentral Property Berhad who issued initial public offering (IPO) of *waqf* of shares on 18th June 2017.

2.4.2   The Management Framework of Malaysian Waqf

Originally, management of *waqf* in Malaysia is the sole responsibility of SIRCs. This however changed when the Ninth Malaysia Plan was tabled and propelled *waqf* to acquire an economic role. Point 70 of the former Prime Minister's speech, Tun Abdullah Ahmad Badawi during the launch of the Ninth Malaysia Plan stated:

Meanwhile, we will continue to develop sources of capital for Bumiputera, for example land and *wakaf* assets currently under the state of Islamic religious authorities. The state Islamic religious authorities need to shoulder the responsibility of *fardu kifayah*, play an active role to develop the economy of Muslims and assist in the development of human capital (Abdullah, 2006, p.36).

Stemming from this, other bodies of *waqf* were created to help assist SIRCs with its development. Figure 2.1 presents the main bodies of *waqf* management in Malaysia.
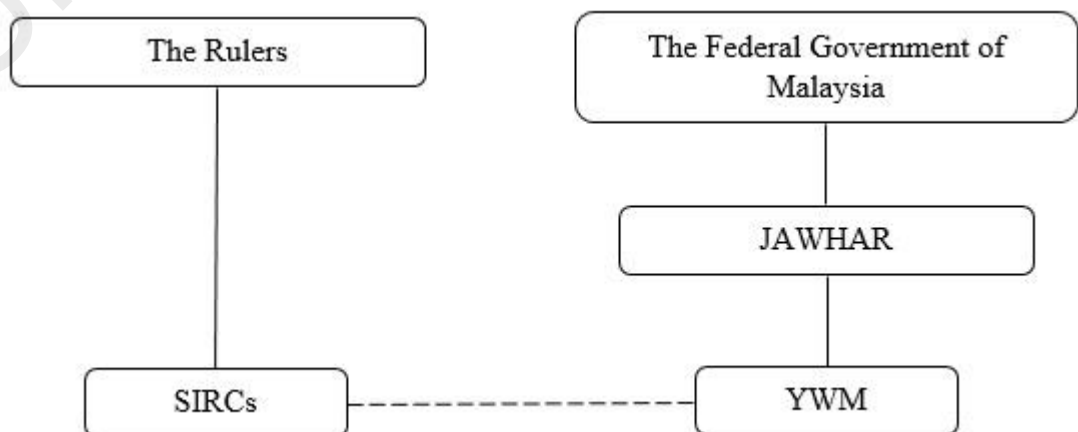
Figure 2.1: The Main Management of *Waqf* in Malaysia

JAWHAR is a department under the Prime Minister's Department comprising of five sections. The section that handles the matters of *waqf* directly is the *Awqaf* section which aims to (JAWHAR, n.d.a):

1. Form smart partnership with government linked companies (GLC)/private and others to develop *waqf* property

2. Plan, execute, and supervise *waqf* property development programme as contained in Malaysia's five-years economic development plan

3. To produce a standard financing and accounting management procedure that SIRC can apply

4. To produce and streamline the development and application of a systematic information technology (IT) and information and communications technology (ICT)

5. Supervise the management and development of *waqf* assets

6. To offer consultancy and facilitate the organisational development and matters regarding *waqf*

7. Conduct research, prepare report, and present confirmation of *waqf* issues

8. To be the secretariat of the national coordination meeting and conference of *waqf*

9. Represent Malaysia in talks and official forum relating to *waqf* matters

10. To carry out high impact projects using federal government fund

11. Form smart partnership with High Networth Individual Muslim in developing *waqf* property through Corporate Social Responsibility programme

On the other hand, YWM is a federal government trust body enacted by JAWHAR in accordance to the Trustees (Incorporation) Act 1952 (Act 258) (YWM, n.d.b). The objectives of YWM are (YWM, n.d.c) :

1. To develop all Malaysian *awqaf* assets through the cooperation of SIRCs as the sole trustees

2. To develop Muslim *awqaf* assets and other Muslim assets for benevolent purposes through the development of economics, education, social, and welfare of Muslims

3. To generate capital using contemporary, advance, and innovative methods in order to maximise *waqf* profits

4. To progressively and productively tackle socioeconomic inequality among Muslims and;

5. To fulfil the will of *waqif*

In addition, YWM also collect *waqf* fund, develop *waqf* assets, carry out welfare, social, and investment program, organise promotional program, and produce publications (YWM, n.d.c). The developments of *waqf* assets are done with other bodies such as SIRCs and universities. In fact, studies are also conducted to develop new *waqf* products.

At the very basic, JAWHAR and YWM undertake the development of Malaysian *waqf* land through federal government funds as provided under the Ninth Malaysia Plan, Tenth Malaysia Plan, and 2010 Budget (Sanep & Nur Diyana, 2011). One question arises; how do JAWHAR and YWM proceed with the development of *waqf* if the sole trustees of *waqf* in Malaysia are the SIRCs? According to Sanep and Nur Diyana (2011), The National Fatwa Council Islamic Affairs of Malaysia that convened on 10th to 12th April 2007 decided that JAWHAR can become a *waqf* trustee through YWM given that both

YWM and SIRCs agree to this arrangement. As the development of *waqf* land is been done in most states, it is safe to assume that YWM and most SIRCs agree to that arrangement. Another vital role that JAWHAR undertakes is the publication of *waqf* manuals. The manuals are *Manual Pengurusan Tanah Wakaf* (Manual of *Wakaf* Land Management), *Manual Pengurusan Peletakhakan Tanah Wakaf* (Manual of Revesting of *Wakaf* Land Management), *Manual Pengurusan Istibdal Wakaf* (Manual of *Wakaf Istibdal* Management), *Manual Pengurusan Perakaunan Wakaf* (Manual of *Wakaf* Accounting Management), *Manual Pengurusan Wakaf Tunai* (Manual of Cash *Wakaf* Management), and *Manual Pengurusan Model Perundangan Wakaf* (Manual of *Wakaf* Legislation Model Management) (JAWHAR, n.d.b). The purpose of these manuals are to promote the best *waqf* management practices in Malaysia. Even though the effort is tremendous for the development of *waqf* in Malaysia, Sharifah Zubaidah (2016) asserted that these manuals need to be updated.

On the other hand, SIRCs are fully responsible for the management of *waqf* in their respective state including financing, accounting, fulfilment of *waqf* deed, and related others. Within this main management framework of *waqf,* there is a need to know who will be the managers of *waqf* to finance public expenditures. Since public expenditures include expenditures in every Malaysian state, will the SIRC be the suitable choice? Does YWM need to enhance its role as a federal trust body? Is there any need to create a completely different *waqf* body? This is a literature gap that this thesis needs to address.

It is wise to mention that the management of *waqf* by SIRCs is often criticised in the literature. Insufficient human resources with knowledge on *waqf* management (Sohaimi & Syarqawi, 2008; Rohayu & Rosli, 2014), lack of transparency (Siraj, 2012; Nazifah & Muhammad Firdaus, 2016), and the time consuming process of endowing *waqf* land (Sharifah Zubaidah & Nor Asiah, 2014; Sharifah Zubaidah, 2016) are among the major

criticisms faced by SIRCs. However, SIRCs also have other responsibilities including matters of *zakat*, *baitulmal*, and other Islamic religious duties (Sohaimi & Syarqawi, 2008) which also require their focus. One of the reasons for lack of transparency is because SIRCs are unable to publish a comprehensive report of *waqf* land data due to the absence of a systematic registration procedures (Rohayu & Rosli, 2014; Sharifah Zubaidah & Nor Asiah, 2014). Plus, there is insufficient accounting standards that can be used by SIRC for *waqf* reporting (Nazifah & Muhammad Firdaus, 2016). Meanwhile, the time consuming process of *waqf* land is because SIRCs must first appraise the land to determine its suitability with the purpose of *waqf* (Anan, 2012).

Aside from these main institutions, another recent institution in Malaysia that has emerged as a manager of *waqf* is the Labuan International *Waqf* Foundations (LIWF). Established in 2015, LIWF is the first international business and financial centre to establish *waqf* using Section 107 of Labuan Islamic Financial Services and Securities Act 2010 (Labuan International Business and Financial Centre [LIBFC], n.d.). The trustees of the *waqf* are the *waqf* foundation itself. LIWF recognises the permissibility of temporary *waqf* whereby the *mawquf* is only endowed within a certain time frame. On top of that, LIWF invites all forms of *waqf* whether it be cash, movable assets, immovable assets, intellectual property rights, and many others within the permissibility of the *Shari'ah*. Of course, Malaysian *waqif* must obtain permission from SIRCs should they want to endow assets in LIWF (LIBFC, n.d.). In addition, various *nazir khas* had been appointed and numerous joint collaborations have been initiated. This has been previously mentioned in Section 2.4.1. As such, it is questionable as whether the *waqf* financing public expenditures should be managed by private *waqf* managers? Or should a joint collaboration be established? Again, these are the questions that this thesis has to answer.

2.4.3   Modes of Waqf Financing in Malaysia

It is only logical to review the modes of *waqf* financing. The very concept of *waqf* that is perpetual in nature can only be safeguarded when financing modes are in place. Hence, the application of *waqf* to finance public expenditure can only remain perpetual when an effective mode of finance is put in place.

In Malaysia, SIRCs employ *badal* or exchange of cash *waqf* and *waqf* shares. The *badal* mode of finance is where cash *waqf* and proceeds from *waqf* shares are collected and pooled together which then exchanged into immovable properties such as land, buildings, schools, hospital etc. by way of purchase (JAWHAR, 2009). The immovable properties become *awqaf* for the beneficiaries to which the next section will highlight a number of examples. This process is depicted in Figure 2.2. However, there are also *waqf* shares that are exchanged into movable *waqf* property. For instance, SIRC Johor had once offered *waqf* shares for the purpose of buying a haemodialysis machine (eWakaf Johor, n.d.).

On the other hand, private *waqf* managers and private sector institutions that collaborated with SIRCs employ partial investment strategies. For instance, WSM invest some of the contributed cash *waqf* in shopping lots to gain return (WSM, n.d.b). This investment is somewhat in line with the recommendation of Çizakça (1998) that cash *waqf* should be invested through Islamic partnership of *mudarabah*. 25 percent from the return on investment (ROI) is channelled to PWS while the remaining 75 percent go to WSM (SC, 2014). The operation of *waqf* finance mode at WSM is illustrated in Figure 2.3.
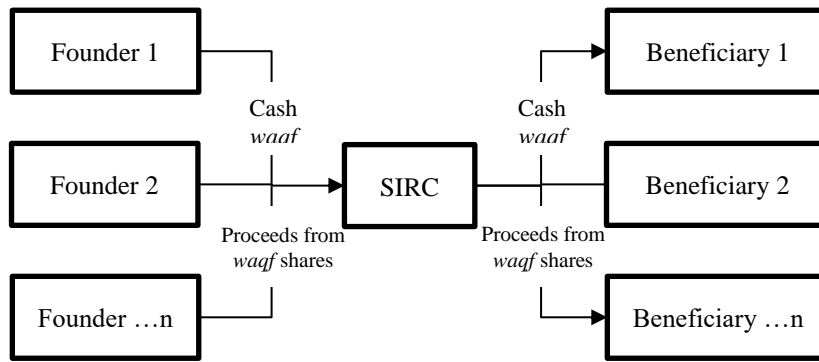
Figure 2.2: The Process of *Badal* by SIRCs
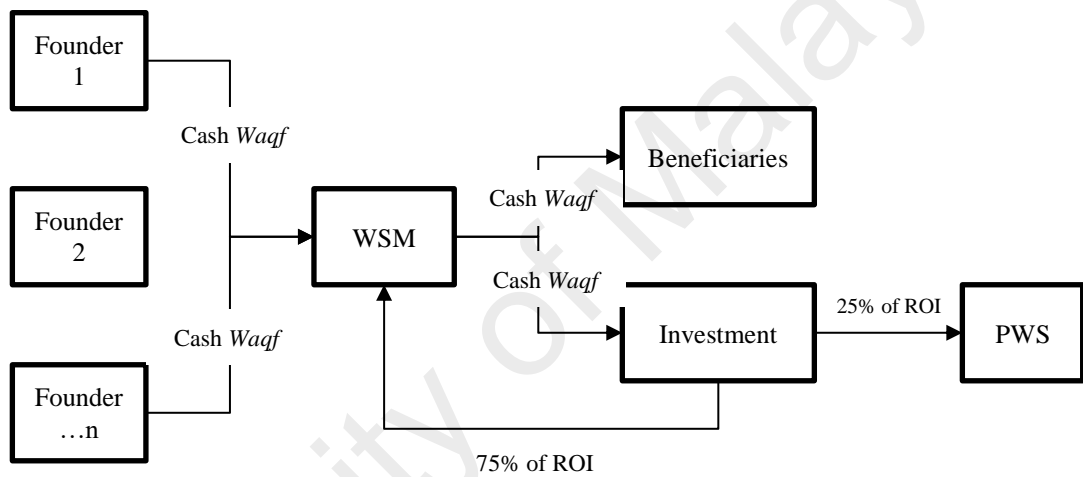
Figure 2.3: The Process of *Badal* and Investment by WSM

On the other hand, JCorp as a *waqif*, employs a complete investment strategy. 7.2% of KPJ Healthcare Berhad, 5.2% of Kulim (Malaysia) Berhad, 2.52% of Al-'Aqar Healthcare REIT, 75% of Tiram Travel Sdn. Bhd., 61% of Larkin Sentral Property Sdn. Bhd., and 75% of Capaian Aspirasi Sdn. Bhd. shares, all of which are subsidiaries of JCORP, are converted into *mawquf* and then reinvested (WANCORP, 2015). The dividends obtained from the investments are then given to the rightful beneficiaries including healthcare, orphans, the poor, entrepreneurs, education, victims of natural disasters, and others. The investment process is illustrated in Figure 2.4.

It is interesting to note that the companies operate in different industries; for instance, KPJ Healthcare Berhad is in healthcare, Kulim (Malaysia) Berhad is in the oil and gas as well as agriculture industry, and Tiram Travel Sdn Bhd is in the tourism industry. Basically, the *waqf* of shares are invested in a diversified portfolio of assets that can minimise risk. This is actually Portfolio Theory at work, whereby return can be maximised by holding a diversified portfolio of assets with different risk levels (Brealey et al., 2011). KAPF, regarded as the leader in *waqf* management, which was discussed in Section 2.3.2.1, also employs the investment diversification strategy. Suggestion for diversification of *waqf* investment is also found in Mohd Umar et al. (2012).
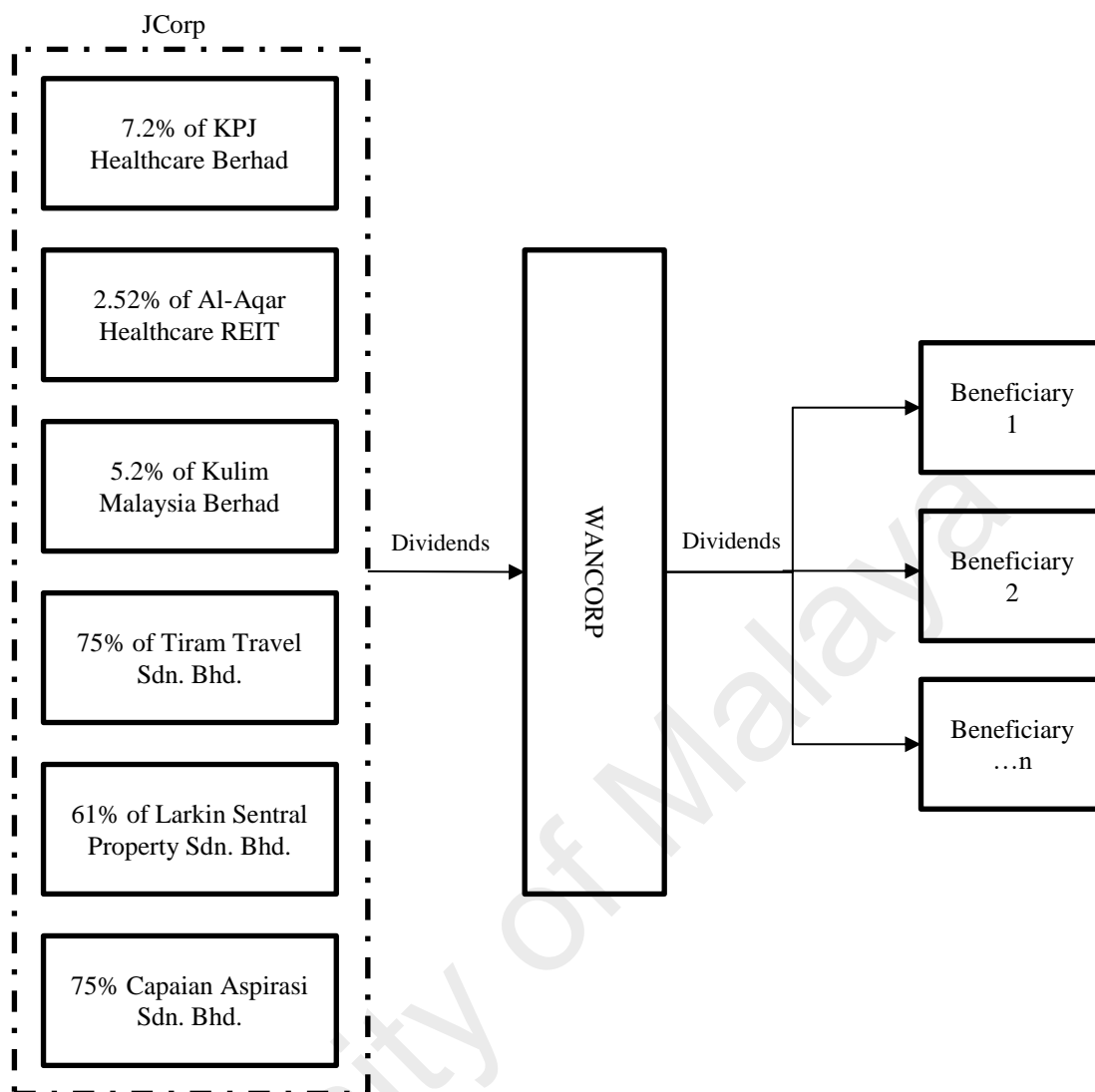
Figure 2.4: Investments of *Waqf* of Shares by JCorp

As a matter of fact, the OIC Fiqh Academy in its Resolution No.140 (15/6) permits diversification of assets. The full conditions for investment of *waqf* funds as detailed in the Resolution are (Mohsin, 2014):

1. The investment must be *Shari'ah* compliant.

2. In order to minimise risk, diversification as an investment strategy should be considered. Risk can also be managed by obtaining surety ships and guarantees, confirming contracts, and performing feasibility studies.

3. Avoid high risk investments. However, it is permissible to invest cash *waqf* through permissible contracts such as *murabahah* (cost plus), *mudarabah* (profit sharing, loss bearing), *istisna'* (order to manufacture), and others.

4. Chosen investment must be suitable to the corpus of *waqf* and duly protects the *waqf* and beneficiary rights. Thus, *mudarabah* mode is allowed due to its compatibility with cash *waqf* despite being considered as a high risk investment.

5. *Waqf* investment activities should be transparent.

Indeed, this is the very definition of *waqf* in economics given by Kahf (2014) in Section 2.2 whereby funds are diverted to investments. However, the real paradigm holds that investment is always associated with risk regardless of how many cautionary steps are taken. An issue thus arises; should the loss incurred from investment despite exhaustion of human intellect be treated the same as immovable property whose value decreases due to disrepair or natural disaster? However, this issue is out of this thesis's scope and thus will not be addressed.

To a certain extent, Mohsin (2013) had provided solutions to this dilemma. In the case of *murabahah* financing mode (low risk investment), it was suggested that 50 percent of the accumulated cash *waqf* is reserved while another 50 percent is invested. From the 50 percent investment portion, 30 percent is invested in low risk investment while the remaining 20 percent is invested in high risk investment. 20 percent from the ROI is then added up to the capital to cushion from any possible losses. Similar strategy is adopted in the case of *mudarabah* (high risk investment) financing mode. In terms of the *musharakah* financing mode (high risk investment), only 10 percent from the 50 percent portion for investment is invested in high risk investment. There is also another solution employed by Larkin Sentral Property Berhad. Stated in their prospectus, the company

will find other sources of finance should the return from the IPO is insufficient (Larkin Sentral Property Berhad, 2017). In other words, if the value of *waqf* capital declines, the manager of *waqf* can offer to compensate the value.

Larkin Sentral Property Berhad is the first to offer an IPO of *waqf* of shares in the country. Its modus operandi is depicted in Figure 2.5. As can be seen, the dividend from the *waqf* of shares is managed by WANCORP where 90 percent of the dividend is channelled to Larkin Sentral Property. The purpose of this *waqf* is to finance the upgrade of Terminal Building of Transport and Public Market at Larkin, Johor Bahru (Waqaf Saham Larkin Sentral, n.d.). These are actually examples of pure and mixed public goods.
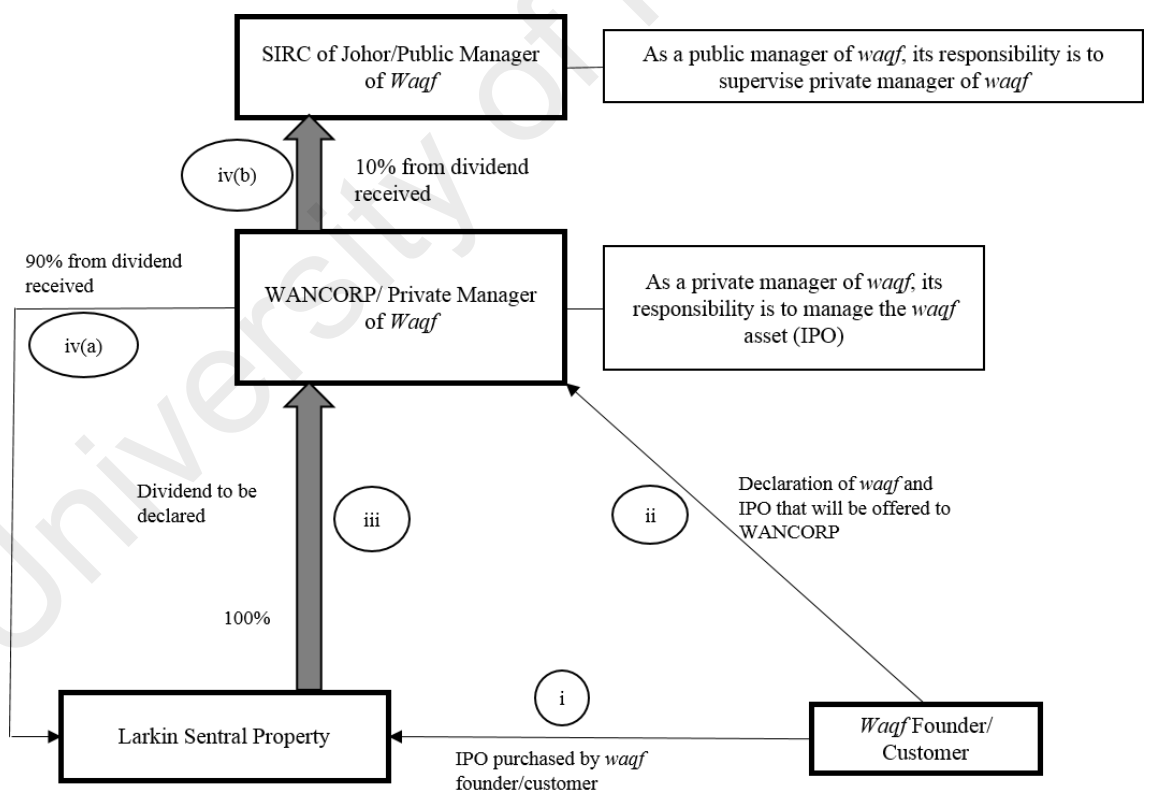
Figure 2.5: The Process of *Waqf* of Shares offered by Larkin Sentral Property Berhad

Source: Larkin Sentral Property Berhad (2017)

The literature has also offered other suggestions to finance the existing Malaysian *waqf* assets. Siti Mashitoh, Asmak, Hasnol Zam Zam and Syarqawi (2007) as well as Aznan and Syahnaz (2016) suggested the adoption of *waqf* Islamic real estate investment trusts (I-REITs). I-REITs is a collective investment scheme that pools money from investors to buy, manage and sell real estate in which the tenants operate *Shari'ah* compliant activities (Securities Commission Malaysia [SC], 2014). Aznan and Syahnaz (2016) proposed a structure of *waqf* I-REITs which is depicted in Figure 2.6. Non *waqf* assets are injected into *waqf* REITs to retain the inalienability principle. This said *waqf* REITs is sponsored by SIRCs. The units of *waqf* REITs are then offered to investors whose proceeds are then used to buy *Shari'ah* compliant assets. These assets are leased back to SIRCs and SIRCs will sublease the assets to *Shari'ah* compliant tenants. Return from the tenants are distributed to the investors, while dividend from *waqf* REITs will be used to develop existing *waqf* assets that are not included in *waqf* REITs.
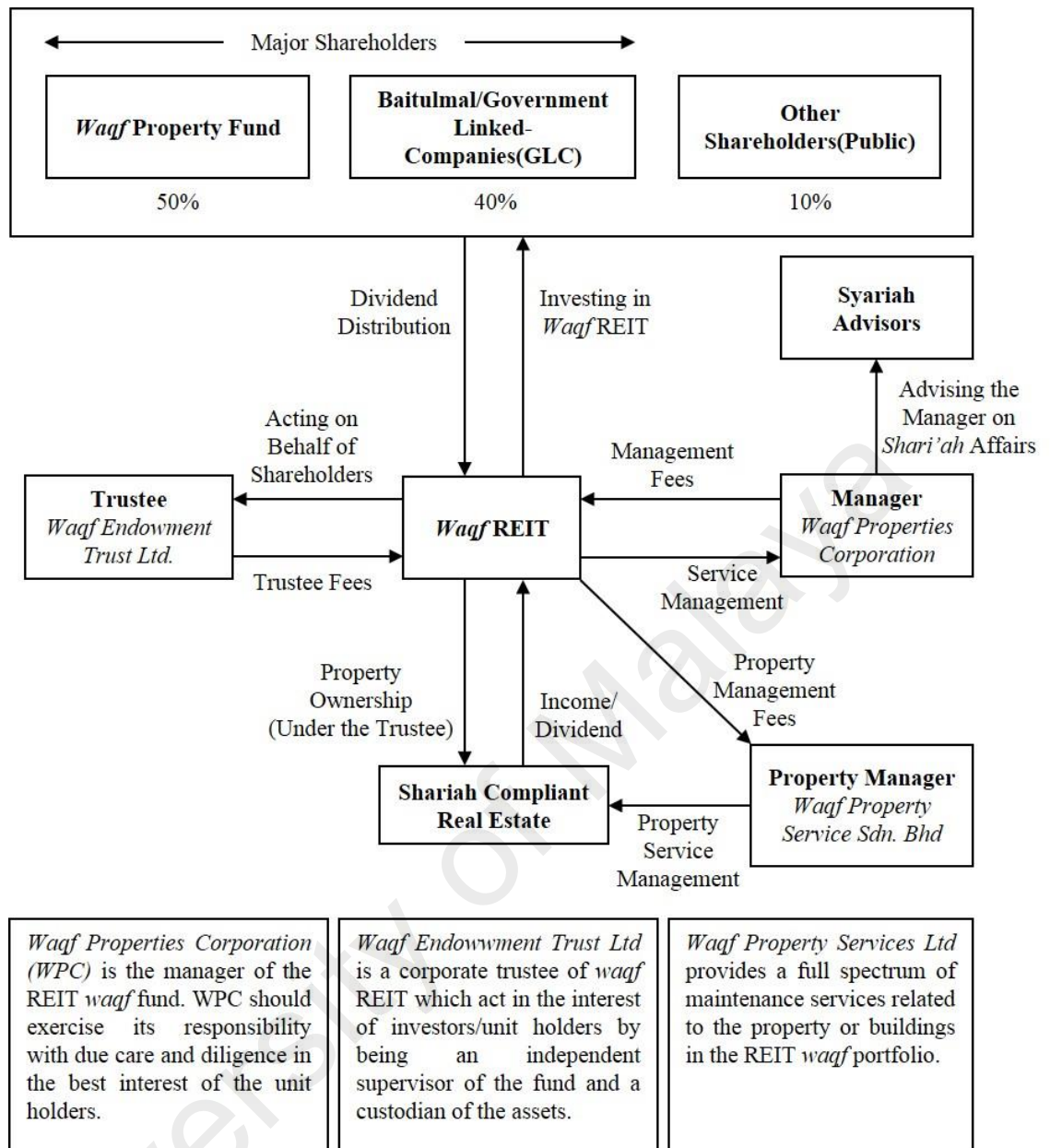
Figure 2.6: Proposed Structure of *Waqf* REITs

Source: Aznan and Syahnaz (2016)

Regarding this, the SC suggested that *waqf* employ the Islamic capital market products as a mode of *waqf* financing (SC, 2014). Examples of Islamic capital market products include *sukuk*, Islamic unit trust, *Shari'ah* compliant shares, Islamic real estate investment trust (I-REITs), and Islamic exchange-traded funds. SC is prepared to regulate *waqf* assets in question that comply with SC's prepared guidelines such as the Guidelines on Unit

Trust Funds, Guidelines for I-REITs, and several others. The support of SC is proven through the issuance of Larkin Sentral Property Berhad's IPO in the form of *waqf* of shares that is regulated by SC Larkin Sentral Property Berhad. Hence, with all the recommendations and modes of financing adopted by SIRCs and *nazir khas*, it is of important that this thesis determines the most suitable technique for *waqf* of public expenditures in Malaysia.

2.4.4   Public *Waqf* in Malaysia

Albeit the lack of public awareness on *waqf* (Mohamad Zaim Isamail, Muhammad Ikhlas Rosele, & Mohd Anuar Ramli, 2015), creation of *waqf* that is economic and socio economic in nature are on the rise. The official website of JAWHAR has a record on the list of *waqf* lands that were developed using the federal government fund in various states of Malaysia for these purposes (JAWHARc, n.d.). The developments include shop lots in Perlis, orphanage in Kedah and Kelantan, hotel and student hostel in Terengganu, low cost housing units and Islamic school complex in Pulau Pinang, hotel and business space in Perak, *waqf* complex which is still under construction in Selangor, hotel and complex for new Islamic converts in Negeri Sembilan, hotel in Malacca, and haemodialysis centre and women shelter in Johor. Meanwhile in Sarawak, no *waqf* land was developed but the federal government fund was used to buy equipment for an Islamic complex while no development was undertaken in Sabah.

SIRCs that enacted *waqf* enactments is observed to have more developments of public *waqf*. As was stated previously, these SIRCs are Johor, Perak, Negeri Sembilan, Selangor, and Malacca. Funds from these projects are largely sourced from the general public. However, no information was obtained on the public *waqf* in Malacca. There are bazaars, marts, healthcare, and student facilities in Negeri Sembilan (PWNS, n.d.; Center for

Awqaf and Zakat, n.d.); residential housing units, healthcare, business complex, and schools in Selangor (PWS, 2011-2014; PWS, n.d.; WSM, n.d.c); haemodialysis centre, boats for fishermen, business centre, and residential colleges in Perak (*Waqaf* Perak Ar-Ridzuan, n.d.); as well as healthcare, *waqf* fund for university, bus terminal, and school buildings in Johor (eWakaf Johor, n.d.).

Actually, all the elaborated public *waqf* are consistent with public expenditure components. These public *awqaf* can be categorised into housing, health, education, trade and industry, agriculture and rural developments, as well as social and community services. These are basically the components of federal government development expenditure (Bank Negara Malaysia [BNM], 2016). Furthermore, the National Higher Education Strategic Plan 2020 had urged public universities to acquire various sources of funding. *Waqf* is one such source. Thus, *waqf* is already an indirect financing of Malaysian public expenditure components. In terms of public expenditure as a whole, will the *waqf* be applicable for all public expenditures? If so, how can it be done exactly? These are the questions that need to be addressed by this thesis.

2.5   The Place for Public *Waqf* in Malaysian Economy

Up to this stage, *waqf* has been reviewed microscopically. However, it is imperative to view public *waqf* in a bigger picture so that the role of public *waqf* can be positioned in modern Malaysian economic setting. This effort can certainly assist with the fulfilment of RO 3. As has been established in Section 2.2, *waqf* is a third sector instrument. Thus, in order to determine the place of public *waqf* in Malaysian economy, it is only sensible to understand the place of the third sector in modern economics. As claimed by Mohd Nahar and Mohamed Aslam (2016), the most dominant third sector framework and the most compatible with *waqf* is the European's third sector framework.

Pestoff (1992) developed a specific framework of European third sector to which Evers and Laville (2004) as well as Defourny and Pestoff (2008) claimed as the best representation by far. The framework, the third sector in the welfare triangle, is depicted in Figure 2.7. The outer shape namely the welfare triangle indicates two things (Evers & Laville, 2004). First, each vertex denotes the sources of welfare contribution namely the state, market, and community. Second, the triangle shows that the third sector is not juxtaposed with the state, market, and community but is in fact an intermediary sector. Meanwhile, the inner circle comprises of third sector organisations (TSOs). These TSOs are "simultaneously influenced by state policies and legislation, the values and practices of private business, the culture of civil society and by needs and contributions that come from informal family and community life" (Evers & Laville, 2004, p.15). The limits of these influences are defined using three types of dotted lines outlining the behaviours of state, market and community while at the same time forming overlapping areas.

The overlapping area between the state and the third sector indicates the role that TSOs have in implementing public policy which are public, non-profit, and formal in nature. Meanwhile, the overlapping area between the market and the third sector involves third sector enterprises like cooperatives which are private, for profit, and formal in nature. The final overlapping area points to self-help or mutual-aid groups that often exist in community which are informal, private, and non-profit in nature. It is crucial to note of other overlapping areas in the small triangles. The small triangle on the left represents informal partnerships between public agencies, while the triangle on the right represents public enterprises with profit motives, and the final represents private informal initiatives.
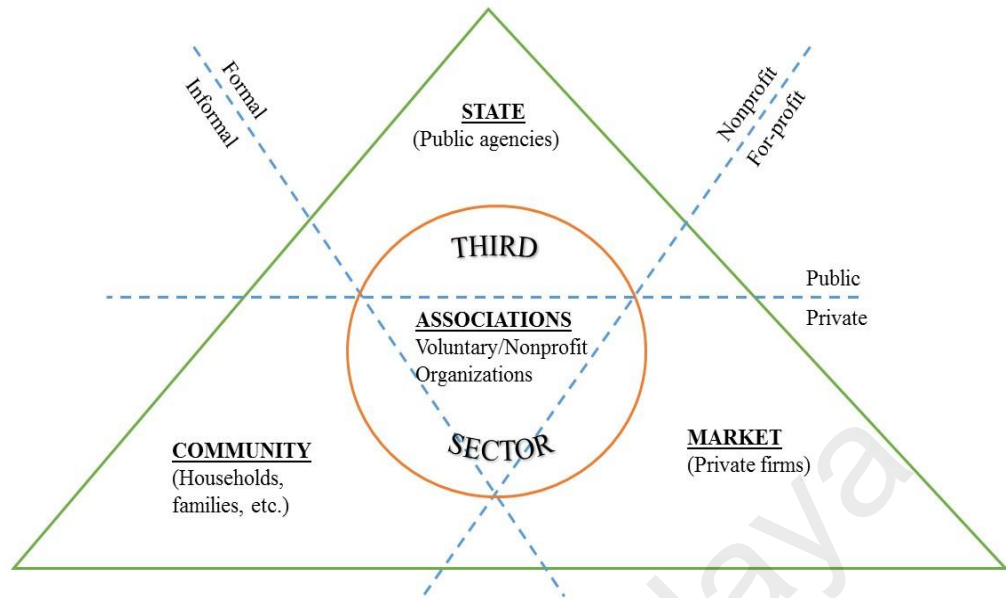
Figure 2.7: The Third Sector in the Welfare Triangle

Source: Pestoff (1992)

It is to the believe of Mohd Nahar and Mohamed Aslam (2016) that the overlapping area between the community and third sector is the only place where *waqf* endowment fits in. However, public *waqf* also fits in between the overlapping area between the state and third sector as well as between the market and third sector. This is because apart from the general public of Malaysia (community), the Malaysian federal government (state) and JCORP (market) also endow public *waqf* in the form of allocated budget and *waqf* of shares, respectively. However, it is hasty to conclude that Figure 2.3 is the best framework for public *waqf*. In studying this framework deeper, it is hard not to realise that certain modifications have to be made to suit public *waqf*. Firstly, the overlapped areas broadly explain the various types of TSOs but *waqf* for public expenditures is considered as a specific type of third sector instrument namely public *waqf*. Secondly, Figure 2.7 considers other overlapping areas (the small triangles) that do not concern with public

waqf. Thirdly, Figure 2.7 explains the state, community, market, and TSO as merely welfare contributors whereas they are also economic agents in the real practice.

This place for public *waqf* is shown in Figure 2.8. As can be seen, the three inner triangles depicting the state, community, and market are separated by dotted lines. These lines highlight the various initiative by the Malaysian federal government, firms, and general public to endow *waqf*. On top of that, these three inner triangles expectedly form an outer triangle. Public *waqf* is placed in a circle that also touches the sides of this outer triangle. This outer triangle represents the economy; hence the state, community, market, and public *waqf* are actually economic agents. The public *waqf* circle also intersects with areas of the other three agents' triangles. These intersections actually delineate the intermediary role of public *waqf* with the three agents. Interaction between all four agents forms an economy.

Here is how the four agents interact. Most public *awqaf* are endowed by the community but tend to be supervised by a public agency, the state for that matter. To reiterate, KAPF is under the aegis of Minister of *Awqaf* and Islamic Affairs, Egypt is under the EAA that reports to the Ministry of *Awqaf*, Singapore is under MUIS, and Malaysia is under the SIRCs. The collected *waqf* endowments are then invested in firms to generate return as is with *waqf* from the economics perspective (Kahf, 2014). For instance, BMMB that collaborates with PWS to manage Selangor's *waqf* invests *waqf* endowments in a wholesale business complex while low yield *waqf* property in Singapore acquires return by buying shares of high yield property. It is from these returns that beneficiaries get to enjoy public *awqaf* and the returns also ensure the continuous operation of public *awqaf* properties. On a side note, areas of the inner triangles that do not intersect with the public *waqf* circle represent the typical roles of economic agents.
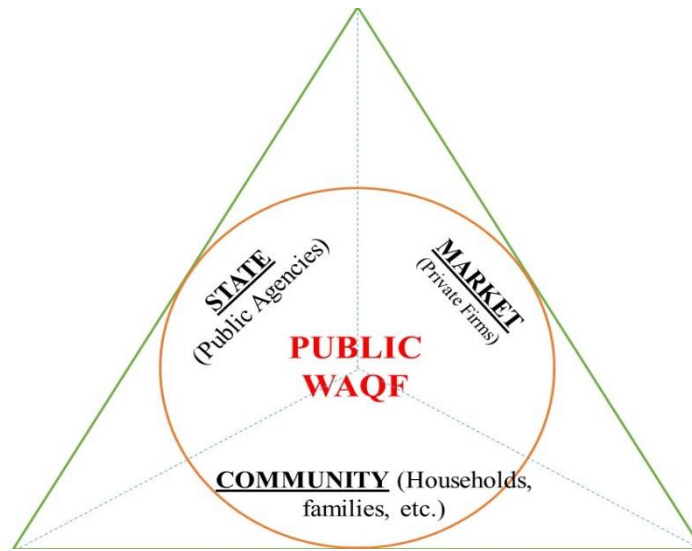
Figure 2.8: Public *Waqf* in the Malaysian Economy

2.6   Conclusion

This chapter has found several literature gaps and issues that need to be addressed. Firstly is the viability of *waqf* to finance Malaysian public expenditures. Although it is found that *waqf* has been financing components that are from current public expenditure and had even become a state policy in the past, more evidence should be obtained to confirm this fact. Secondly is the proper mode of finance that *waqf* for Malaysian public expenditures can adopt. There were many modes of finance described in the literature, but deeper investigation needs to be carried out to determine the best strategy. Thirdly is the management for the *waqf* in question. *Waqf* laws are different from state to state, thus this thesis has to find out a way to facilitate the operation of *waqf* for public expenditure. This thesis also has to figure out who will be the managers for the *waqf* in question. Apart from these literature gaps, Chapter 2 was able to situate the role of *waqf* in the Malaysian economy. Such acknowledgement was made by reviewing the European third sector framework and harmonising it with the practice of Malaysian *waqf*.

CHAPTER 3: MALAYSIAN FEDERAL GOVERNMENT EXPENDITURE AND THE GROWING DEBT

3.1 Introduction

This chapter discusses the literature pertaining to the Malaysian federal government expenditure and debt in depth. As expounded in Chapter 2, *waqf* had provided public goods and other social services in the past. Hence a dissection of the Malaysian federal government expenditure is done to determine which expenditures are suitable for *waqf* to cater and appealing to potential *waqif*. This is also important to clarify the purpose of *waqf* to potential *waqif* and make (s)he to understand that his or her endowments do positively impact the public. It also coincides with impact philanthropy whereby an endower prefers to contribute to a specific good rather than across multiple goods (Duncan, 2004). Since this thesis also studies the impact of *waqf* financing certain expenditures on debt, literature on government debt with a special focus on the Malaysian federal government debt are reviewed.

Basically, this chapter is organised as follows. Section 3.2 presents the condition and a comprehensive review on the Malaysian federal government expenditure components in regard to *waqf*. Section 3.3 focuses on the condition of Malaysian federal government debt and its components. Section 3.4 highlights government debt from the perspective of conventional and Islamic economics. Section 3.5 explains the strategies that can be taken to sustain or reduce government debt. Methods to evaluate government debt are then reviewed in section 3.6. Finally, a conclusion is presented in section 3.7.

3.2 The Federal Government Expenditure and Its Components

The general aim of this section is to identify the expenditures that are suitable for *waqf* to finance. Briefly, federal government expenditure is incurred when the federal

government mobilises its finances to carry out the tasks or responsibilities within its jurisdiction. The jurisdiction of the federal government can be found in the Federal Constitution of Malaysia. The Federal Constitution separates the jurisdiction into two lists; one that is solely borne by the federal government (federal list) and another jointly borne with the state government (joint list). The federal list includes foreign affairs, defence, security, finance, government machinery, carpentry, trade and industry, shipping and fisheries, transportation and communication, road works, water supply, power and gas, research and education, labour and labour protection, the welfare of aborigines, and others. Meanwhile, the joint list includes among others, scholarship, wildlife conservation, health, culture and sports, as well as community welfare.

BNM (2016) group the federal government expenditures into two broad categories; the operating expenditures and the development expenditures. Figure 3.1 depicts these categories of federal government expenditures. The operating expenditure include emoluments, pension and gratuities, debt service charges, supplies and services, subsidies, asset and acquisitions, grants and transfers, as well as other expenditures. Meanwhile, development expenditures include defence and security, economic services, social services, and general administration. A cursory look at Figure 3.1 suggests that development expenditure is the most appropriate for *waqf* financing as its components directly benefits the public, except for general administration and trade and industry.

Federal Government Expenditure

Operating Expenditure

Development Expenditure

1. Emoluments
2. Pension and gratuities
3. Debt service charges
4. Supplies and services
5. Subsidies
6. Asset acquisition
7. Grants and transfers
8. Other expenditure

Defence and security

Economic services

1. Agriculture and rural development
2. Trade and industry
3. Transport
4. Public utilities
5. Others

Social services

1. Education
2. Health
3. Housing
4. Social and community services

General administration

Figure 3.1: Components of Malaysian Federal Government Expenditure

Source: BNM (2016)

However, development expenditure is small as oppose to operating expenditure (refer to Figure 3.2) suggesting that the latter is more in need of *waqf* financing. The problem is, it is highly unlikely for persons to endow *waqf* for federal government operation because it is difficult for (s)he to view said purpose as the greater good. One way or another, the federal government expenditure problem needs to be addressed because it is in fact persistently large. This is demonstrated in Figure 3.3 whereby persistent primary deficit has been occurring since the year 2008. A closer scrutiny on each of the expenditure components is again necessary.
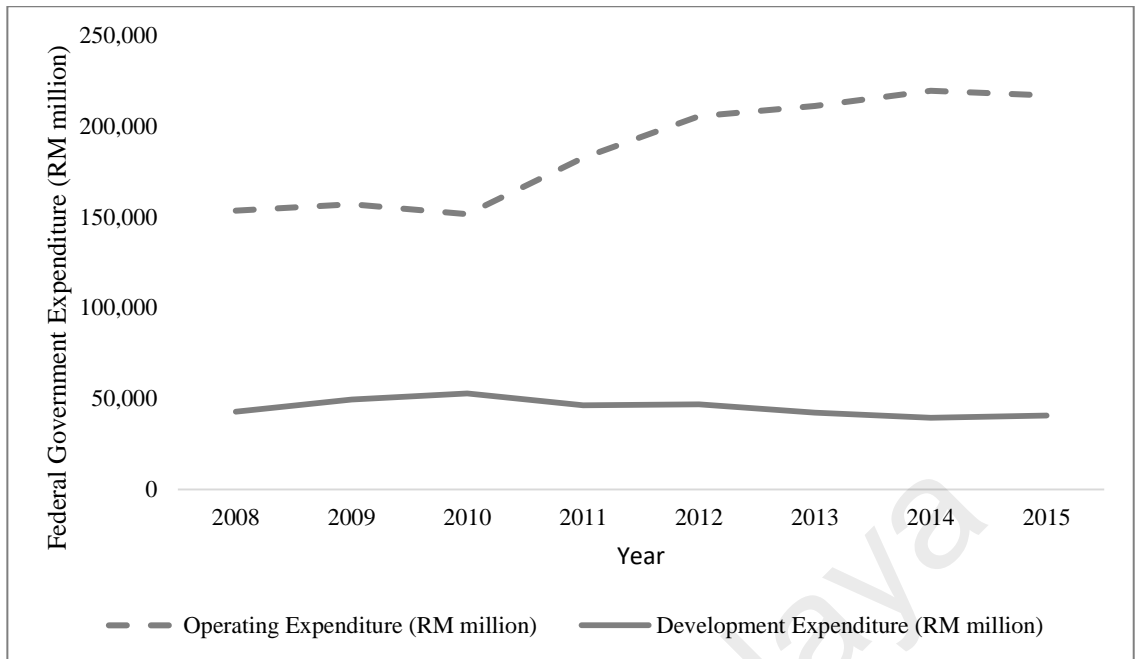
Figure 3.2: Broad Components of Malaysian Federal Government Expenditure
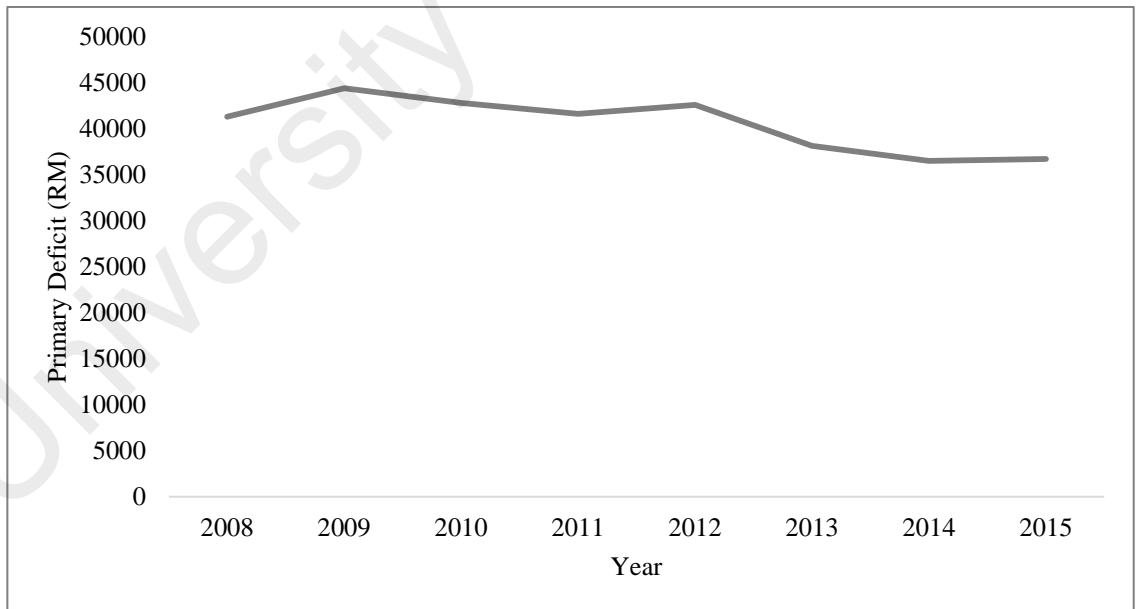
Source: BNM (2016)

Figure 3.3: The Primary Deficit of the Malaysian Federal Government

Source: BNM (2016)

3.2.1 Federal Government Operating Expenditure

Figure 3.4 presents the breakdowns of the operating expenditure components. Emoluments account as the largest at 32% while asset acquisition and other expenditure account the least at 1%. A detailed account on operating expenditure of year 2015 can be obtained from the Economic Report produced by MOF Malaysia (2015/2016). Emoluments constitute salaries, annual salary increment, and financial assistance making these items highly unlikely to receive *waqf* endowments. Grants and transfers as well as supplies and services account for 17%. The former is allocated to public universities, agricultural development authorities, trade and investment promotion agencies, and state governments. Grant to public universities fosters research and agricultural development authorities aid farmers, thus, these items should be suitable for *waqf* financing. However, it must be noted that it is almost impossible to obtain isolated values of grants for public university and agricultural development authorities. This can affect the thesis analysis. Meanwhile, supplies and services are not suitable for *waqf* financing as they constitute repairs, maintenance, and payment for services rendered.
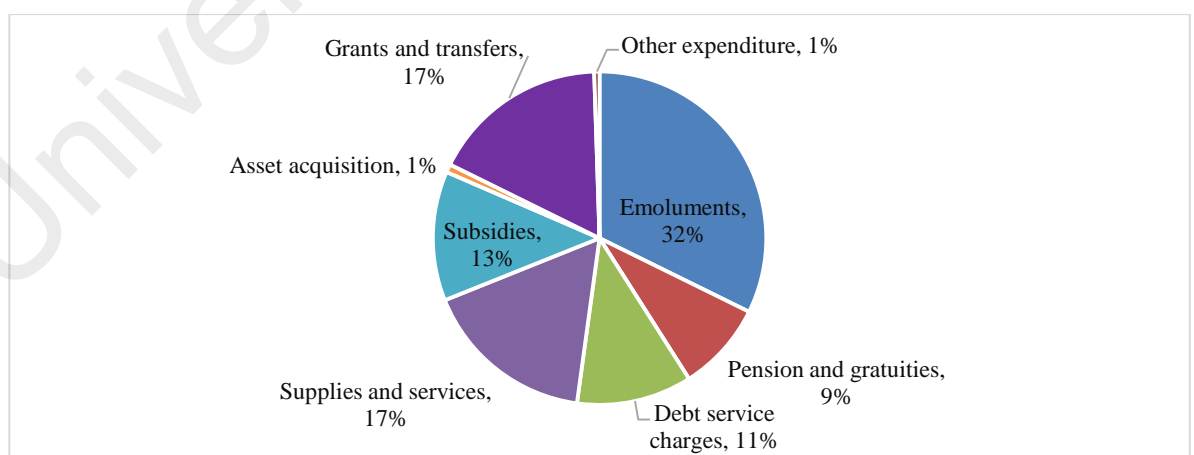
Figure 3.4: Components of Malaysian Federal Government Operating Expenditures in Year 2015

Source: BNM (2016)

Subsidies stand at 13% comprising of assistance and incentives encompassing cash assistance, educational assistance, incentives for farmers and fishermen, cooking oil subsidy, toll compensation, as well as fuel subsidies for public transport, fishermen, and liquefied petroleum gas. As subsidies directly affect the public, *waqf* endowments is especially probable. Debt service charges is at 11%. Since this require the payment of interest, *waqf* is not permitted from the *Shari'ah* point of view to finance this item. Pension and gratuities or retirement charges hold 9% of the overall operating expenditure and is improbable for *waqf* financing. Asset acquisition has a high chance to not obtain any *waqf* endowment simply because it does not directly benefit the public. Lastly, other expenditures include refunds and write offs, grants to international organisations, insurance claims, gratuities, and others (BNM, 2016) which are not suitable for *waqf* financing.

3.2.2   Federal Government Development Expenditure

The economic services take up 57% of the overall development expenditure and make up the largest component, followed by social services at 27%, defence and security at 12%, and general administration at 4% (refer to Figure 3.5). A detailed account on operating expenditure of year 2015 is obtained from the economics report produced by MOF Malaysia (2015/2016). Defence and security involve the protection of public safety which includes safeguarding national border and security as well as enhancing internal security. As they constitute a public good, *waqf* endowments for defence and security are suitable. General administration consists of upgrading ICT and application systems in government departments and land acquisition; plus, building, refurbishment, and maintenance of government facilities. In this regard, *waqf* endowments might not be suitable because *waqif* will not see the significance of contributing for general

administration. The truth is, just like any other bodies, there is also a cost for *waqf* administration or management. Economic services and social services on the other hand, can be broken down further.
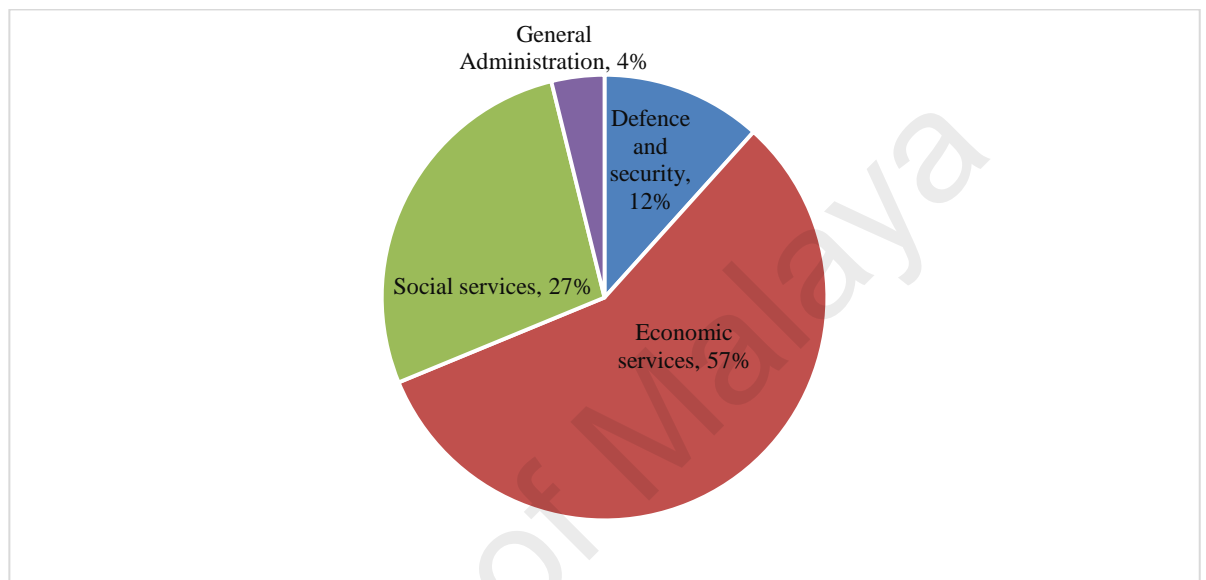
Figure 3.5: Components of Malaysian Federal Government Development Expenditures in Year 2015

Source: BNM (2016)

Figure 3.6 shows the items in economic services. Transport is the largest at 29% followed by trade and industry at 24%, others at 18%, public utilities at 16%, and agricultural and rural development at 13%. Transport consists of construction, maintenance, and upgrade of roads, bridges, railways, ports, and airports. This directly benefit the public so is suitable for *waqf* endowments. Trade and industry focuses on projects that promote trade activities to generate further income for Malaysia. This include entrepreneurship development programmes, palm oil industrial cluster, eco-tourism projects, and other projects that promote economic growth. Trade and industry is deemed suitable for *waqf* endowments because as we have seen in Section 2.4.3, there

are cash *waqf* schemes collected by SIRCs for shop lots purchase and *waqf* endowments by the federal government to build hotels on *waqf* land. In other words, *waqf* made to finance trade purposes is allowed to which the income gain is channelled to purposes that directly benefit the public.
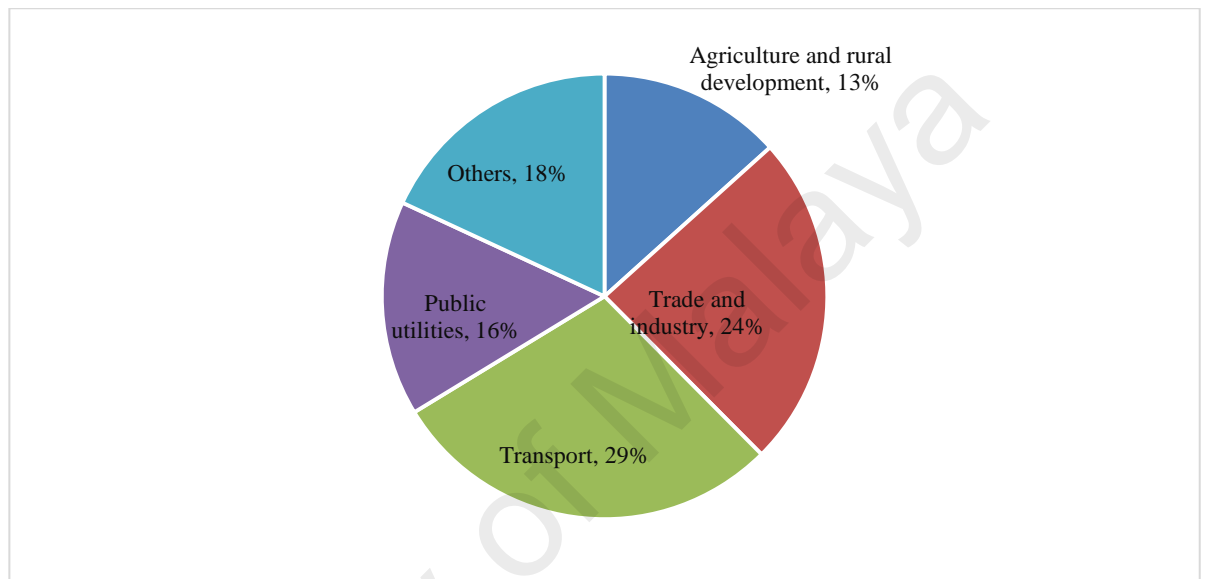
Figure 3.6: Economic Services Components

Source: BNM (2016)

Public utilities encompass water supply, electric supply, and sewerage system that are of benefit to the public. Therefore, *waqf* endowment is highly suitable for public utilities. Agriculture and rural development is also suitable for *waqf* endowment because it directly concerns the public. Others include miscellaneous items that are associated with the economic sector. Since the economic sector is overall beneficial to the public, whether it be a way for generating revenue or is a direct benefit to the public, others should be suitable for *waqf* too. Figure 3.7 depicts the social services components. Education make up the largest at 43%, social and community services at 26%, housing at 18%, and health at 13%. Education consists of university buildings expansion, construction of schools and

training institutes, equipment upgrading, enhance skills training, and research programmes. It is without doubt that education is definitely suitable for *waqf* endowment. Housing consists of constructing affordable and quality homes for the middle and lower income group. This automatically qualifies for a *waqf* endowment.
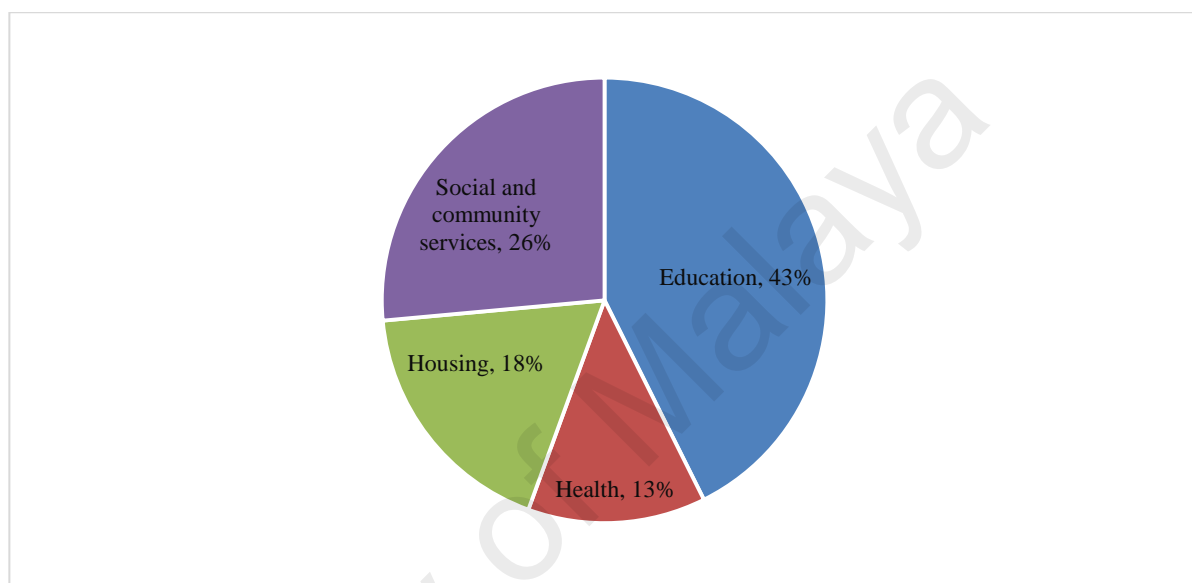
Figure 3.7: Social Services Components

Source: BNM (2016)

Health involves among others, the construction of additional hospital buildings, acquisition of ambulances, and provision of mobile clinics according to MOF Malaysia (2016/2017). There is no explanation on social and community services in MOF Malaysia (2016/2017) nor MOF Malaysia (2015/2016). However, an explanation is found in MOF Malaysia (2010/2011). According to the report, social and community services involve expenditure in upgrading and building parks and recreational facilities, solid waste management, welfare services for the elderly and other vulnerable groups, flood prevention projects, rehabilitating rivers, and fire-fighting services. These are all public goods and can thus be the rightful beneficiaries of *waqf*.

3.3 The Federal Government Debt

As the topic of this thesis also concerns Malaysian federal government debt, it is only called for to review the aspects related to it. The amount of federal government debt and their respective categories are recorded in the Monthly Statistical Bulletin published by BNM. Federal government debt constitutes of domestic debt and external debt. Domestic debt is further categorised into Treasury Bills, Investment Issues, Government Securities, and other loans while external debt comprises of market loans and project loans. These breakdowns are shown in Figure 3.8.
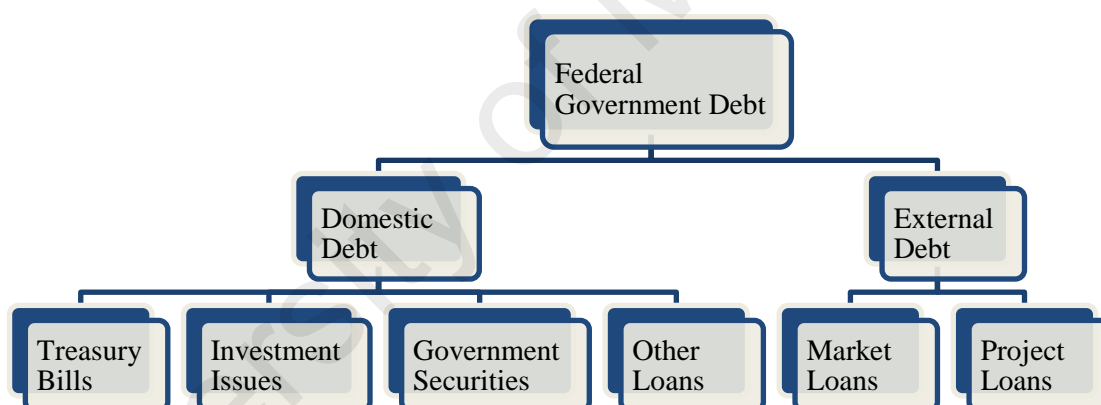
Figure 3.8: Breakdowns of the Malaysian Federal Government Debt

Source: BNM (2016)

Treasury bills are held by BNM, banking institutions, foreign holders, and others. Meanwhile, investment issues or more widely termed as government investment issues (GII) are held by the Employees Provident Fund (EPF), Kumpulan Wang Amanah Persaraan (KWAP), insurance companies, BNM, banking institutions, development financial institutions, non-bank financial institutions, foreign holders, and others. On the

other hand, government securities or widely known as the Malaysian government securities (MGS), are also held by Employees Provident Fund (EPF), Kumpulan Wang Amanah Persaraan (KWAP), insurance companies, BNM, banking institutions, development financial institutions, non-bank financial institutions, foreign holders, and others. Lastly, other loans mainly include loans to the Housing Loans Fund, market loans[1], issuance of *Sukuk Simpanan Rakyat*[2], and *Sukuk 1Malaysia*[3] and *Wakala* Global *Sukuk*.

On the other hand, details on the sources of the federal government's external debt were obtained from the Economic Reports published by the MOF Malaysia. Market loans were supplied by the international capital market. Specifically, the Government had issued bond and *sukuk* such as the Global Bond in 1999 and the Global *Sukuk* in 2010 at the international capital market to raise money. Meanwhile, project loans were obtained from bilateral and multilateral institutions such as the Overseas Economic Cooperation Fund (OECF) and the World Bank (MOF Malaysia, 1999/2000). The main holders of each categories of the Malaysian federal government debt are depicted in Table 3.1.

Since the year 2008 until the year 2014, domestic debt represents the major part of the Malaysian federal Government debt (refer Table 3.2). According to the Economic Reports of 2009/2010 to 2014/2015 borrowings are sourced domestically because there is ample liquidity in the financial market. However, since the year 2009 the domestic debt has been slowly declining while the external debt is steadily increasing. This can clearly

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[1] Beginning from first quarter 2008

[2] Issued in May 2009 and has matured in 2012

[3] Issued in May 2010 and has matured in 2013

be seen from the relative decrease in the ratio of domestic debt to external debt which is

from 5.14 in year 2008 to 2.47 in year 2014.

Table 3.1: Major Holders of the Malaysian Federal Government Debt (BNM, 2016; MOF Malaysia, 2009/2010, 2010/2011, 2011/2012, 2012/2013, 2013/2014, 2014/2015)

Domestic Debt		
Treasury Bills	• BNM • Banking institutions • Foreign holder • Others	
GII	• EPF • KWAP • Insurance companies • BNM • Banking institutions • Development financial institutions • Non-bank financial institutions • Foreign holders • Others	
MGS	(Similar to GII)	
Other Loans	• Housing loans fund • Market loans • *Sukuk Simpanan Rakyat*	• *Sukuk 1Malaysia* • *Wakala* Global *Sukuk*
i. **External Debt**		
ii. Market Loans	• Global Bond • Global *Sukuk*	
iii. Project Loans	• OECF • The World Bank	

Table 3.2: The Malaysian Federal Government Debt Figures (BNM, 2016)

Year	Total Debt (RM million)	Domestic Debt (RM million)	External Debt (RM million)	Domestic Debt to Total Debt	External Debt to Total Debt	Ratio of Domestic Debt to External Debt
2008	306,437	256,512	49,925	83.71%	16.29%	5.14
2009	362,386	306,477	55,909	84.57%	15.43%	5.48
2010	407,101	315,344	91,757	77.46%	22.54%	3.44
2011	456,128	333,755	122,373	73.17%	26.83%	2.73
2012	501,617	352,359	149,258	70.24%	29.76%	2.36
2013	539,858	381,426	158,432	70.65%	29.35%	2.41
2014	582,828	414,675	168,153	71.15%	28.85%	2.47

The purposes of borrowings are documented in the Malaysian Economic Reports. Between the years 2009 and 2014, the borrowings are undertaken to pay down existing debt, and finance ongoing projects and programmes related to education and training, power generation, water supply, sewerage services, ICT infrastructures, and rail transport. Excluding paying down existing debt, these items are basically pure and mixed public goods. Hence it is permissible for *waqf* to finance these items. In addition to these, the borrowings were meant to promote Malaysia as a global Islamic financial hub through the issuance of *sukuk*. In particular, the government had issued the 1Malaysia retail s*ukuk*, sovereign *sukuk,* the *Wakala* Global *Sukuk*, and GII based on the *Murabahah* structure throughout the said period. However, *sukuk* is still a debt based instrument that adds to the amount of federal government debt. Perhaps Malaysia can opt instruments that are based on the concept of *waqf*.

Anyhow, these borrowings have caused an increasing trend in the federal government debt to GDP ratio (refer Figure 3.9). According to Akyuz (2007), majority of past studies had stated that the debt to GDP ratio threshold for developing economies is at 50%. Thus, the debt to GDP ratio figures show that the Malaysian Federal Government debt at the later years of 2009 has put a strain on the country. Should *waqf* cater for those

expenditures that are permissible, then the federal government can reduce borrowing and hence, the debt. It is also interesting to point out that the sharp rise in debt to GDP ratio occurred during the global economic crisis; between 2008 and 2009 which suggests that Malaysia is quite vulnerable to external crisis. Should Malaysia be able to apply *waqf* for financing certain federal government expenditures, which is an internal financing source that incurs zero debt, then Malaysia's vulnerability to external crisis can be contained.

Figure 3.9: The Malaysian Federal Government Debt to GDP ratio

Source: BNM (2016)

3.4   The Conventional and Islamic Perspective on Government Debt

It is interesting to examine the view of debt from both the conventional and the Islamic perspectives. Both viewed excessive government debt as unfavourable. This section coincidentally lays the argument for the dangers of excessive debt which is the main trigger for this research.

3.4.1 Conventional Perspective on Public Debt

The bulk of literature on public debt always derive its theories and arguments between the New Classical (NC) macroeconomics and the New Keynesian (NK) economics (Sutherland, 1997; Tsoulfidis, 2007; Sakuragawa & Hosono, 2011; Konzelmann, 2014; Sardoni, 2013; Tourinho, Mercês & Costa, 2013; Panizza & Presbitero, 2014; Teles & Mussolini, 2014). The former school of economics had evolved from Classical economics while the latter had evolved from Keynesian economics. We shall begin the discussion with views of debt from the Classical economics.

Palley (2012) stated that "…the fundamental conclusions of new classical macroeconomics are essentially those of classical macroeconomics" (p.10). Hence, NC economics adopted the Classical's view on public debt. The foundation for Classical economics was laid in a book titled The Wealth of Nation authored by Adam Smith in 1776 (Tsoulfidis, 2010). Public debt was among the topics discussed in his book. Adam Smith asserted that debt accumulation will only result in increased taxation, capital flight, currency devaluation, and crowding out of private investment (Tsoulfidis, 2007, 2010). He also stated that all government expenditures should be financed by taxation instead, and budget deficits are justifiable only in events of emergencies such as wars and natural disasters (Tsoulfidis, 2007, 2010).

Another proponent of Classical economics, David Ricardo, held similar views with Adam Smith. In his opinion, public borrowing deludes individuals from saving more as both interest and principal had to be paid (Tsoulfidis, 2010). Thus, David Ricardo claimed that incurring public debt will slow down capital accumulation as opposed to situation of tax collection. Take note, Classical economists assumed savings are equal to and determine by investments. This fact means deceleration of capital accumulation will lead to fall in income and revenue. In an attempt to raise similar tax revenues, the government

will increase tax rates which further decreases capital accumulation. Thus, national bankruptcy becomes imminent. However according to John Stuart Mills, another Classical Economist, the situation can be reversed if the funds for loan payment are sourced from foreign savings or domestic savings (Tsoulfidis, 2007).

On the other hand, Keynesian economics reject the notion that savings determine investments but claim that it is determined by levels of income. This is only sensible for Keynesians because by that time, the financial system had already been fully developed. In extension, public debt was also viewed differently. Unlike Adam Smith, John Maynard Keynes (the father of Keynesian economics) did not directly express his view on public debt in his main authored book, The General Theory of Employment, Interest and Money. Instead, Keynes's view can be found in the debates between him and Abba P. Lerner in 1940 to 1944 in addition to other comments from him in the 1930s and 1940s. Aspromourgos (2014) summed up Keynes's view as "cautious" though he was not necessarily a "debt conservative". Keynes had the opinion that as long as the income growth of a country supersedes the growth of public debt, then public debt is not a danger to the country.

NK economics evolved from Keynesian economics by also recognising several views from other economics school of thought such as the Ricardian Equivalence Theorem (Greenwald & Stiglitz, 1987; Tsoulfidis, 2010). Sardoni (2013) states that the Keynesian view of public debt can be summarised into three main points; (1) public debt is different than private debt, thus, there is no need to eliminate it at a certain future date, (2) public deficit is necessary if it can guarantee satisfactory level of employment and output, and (3) the study on debt to GDP ratio dynamics should be conducted by including the GDP and its growth in the debt function as well as in the budget function; not independently.

Thus, NK economics adopts the same opinion that Keynes' had on public debt; "cautious" but not necessarily conservative.

Recent studies that examine the consequences of excessive debt usually based their study on NC and NK economics. Motley (1987), Sutherland (1997), as well as Checherita and Rother (2010) found evidence that high government debt results in contractionary effects. The reason being is households are forward looking in that they expect government to increase tax at some point, inducing them to save instead of consuming. Also based on this assumption, Teles and Mussolini (2014) showed how high debt to GDP ratio can constrain the effects of productive expenditures on growth in the long term. On the other hand, Kwon, McFarlane, and Robinson (2009) based their study on monetarism provided strong evidence that rising public debt can cause debt-inflation trap in high indebted developing countries.

3.4.2   Islamic Perspective on Debt

In general, debt is highly discouraged in Islam. This is evident in a tradition of the Prophet Muhammad PBUH narrated by Aisha:

Allah's Apostle used to invoke Allah in the prayer saying, "O Allah, I seek refuge with you from all sins, and from being in debt." Someone said, O Allah's Apostle! (I see you) very often you seek refuge with Allah from being in debt. He replied, "If a person is in debt, he tells lies when he speaks, and breaks his promises when he promises." (Sahih Bukhari, Hadith 582)

However, the case of public debt is quite different. As cited in Bensaid, Grine, Nor, and Yusoff (2013), Imam Nawawi had argued in *Rawdat al Talibin* that the undertakings of debt for public benefit is considered charity in Islam. This statement is strongly

supported by numerous *hadith* listed in Siddiqi (1995). One such *hadith* is as below (Siddiqi, 1995, p.74):

Ismail son of Ibrahim son of Abdullah, son of Abu Rabi'ah Makhzumi has reported to us from his father who reported about his grandfather that when the Prophet (pbuh) was to attack Hunayn he borrowed thirty or forty thousand from him. He repaid it when he came back. Then the Prophet (pbuh) told him: `May Allah bless you with prosperity in your family and your property. The proper recompense for lending is repayment and gratitude.

Furthermore, public borrowing activities also occurred during the period of Umayyad, Abbasid and early fourth century after *Hijrah* (AH) (Siddiqi, 1995). An example from each of the respective periods are stated below:

They took stock of the public treasury and discovered that it had only two hundred thousand dirhams. This was insufficient. Muhallab then sent for the traders and told them: For a whole year, your business is depressed because the supplies from Ahwaz and Persia had been cut off from you. Let us have some transactions. Then you come with me and I will, God willing, fulfil all my obligations toward you. They sold to him and he took whatever he needed to equip his army and to provide for it....... (Siddiqi, 1995, p.71).

We have yet another report about the same year, 323 A.H. This time the *wazir* tried to borrow from traders in order to pay the troops, offering traders letters of credit (*saftajat)*, the traders disappeared and the effort did not succeed. (Siddiqi, 1995, p.76)

The recorded history in public borrowings, especially in the traditions of the Prophet PBUH had brought Siddiqi (1995) to conclude a few facts that are relevant with

the current public borrowings from the Islamic perspective. First, public borrowing is legal and justified when there is a need, even if the borrowings are from non-Muslims. Second, countries should make their borrowings purpose specific in order to appeal to the sense of morality in lenders, thus, motivating the lenders to grant interest free loans. For example, governments can specifically ask for borrowings to finance education development, medical care, and other social services. Third, governments must pay the dues of debt even if it requires further public borrowings. This third fact indicate a correlation of Islamic economics with Keynesian economics that borrowing is not viewed conservatively.

But what of the consequences of public debt from Islamic economics perspective? To the knowledge of this researcher, studies on this area are lacking even though a number of Islamic countries are embroiled in high public debt. According to the World Economic Outlook database provided by International Monetary Fund (2017), the general government debt to GDP ratio of Egypt, Jordan, Morocco, and Yemen are 88%, 93%, 64%, and 67% respectively in 2015. No matter, there are indeed evidence of negative consequences from excessive government debt that was stated at the end of section 3.4.1.

3.5 Strategies to Sustain Government Debt

Given the fact that excessive debt is unfavourable, it is only sensible to review the literature on debt reduction strategies. Plus, increasing trend of debt to GDP ratio that was stated in the problem statement of this thesis and in Section 3.3 should be address. The methods to reduce government debt or sustain it are often derived from the government budget constraint:

$$B_t + T_t = B_{t-1}(1 + R_t^r) + G_t \tag{1.0}$$

The above equation simply states that present debt (B_t) and present tax or revenue (T_t) must be equal to present government expenditure (G_t) and previous debts (B_{t-1}) plus interest (R_t^r). This is obviously true because government finances expenditure and pays past debt plus interest by incurring tax and further debt. Thus, at a glance, we can deduce that government debt can be sustained either by reducing government expenditure or by increasing tax, or both.

The literature on public debt indicates that different conventional schools of economic thought propose different strategies to sustain debt; but still on the basis of Equation 1.0. In fact, one can understand this difference based on the discussion in Section 3.4.1. The NK economics propose that government invest in productive government expenditures while the NC economics recommends that government increase tax. Controlling for the value of interest rate, part of the conduct of monetary policy, is also one technique. There are also techniques that combine multiple variables in Equation 1.0. The final technique is contained in the school of Islamic economics. We discuss each in turn.

NK economics calls for the government to invest in productive government expenditure that can increase economic growth which is high enough to overcome R_t^r (Sardoni, 2013). The end result of this strategy is a manageable government debt. This can be seen in an analysis done by Mabugu, Robichaud, Maisonnave, and Chitiga (2013) for the case of South Africa where increase in government's investment expenditure translates into reduced debt to GDP ratio. Neck and Sturm (2008) visualises this debt stabilisation by dividing the variables in Equation 1.0 with gross domestic product (GDP) and rearranging to get:

$$b_t = \hat{s}_t + \frac{1 + R_t^r}{1 + y_t} b_{t-1} \qquad (1.1)$$

whereby b_t is debt over GDP, $\hat{s}_t$ is primary balance over GDP, and y_t is the growth rate of GDP. From this we can deduce that the ratio of debt to GDP increases when two situations occur simultaneously, a primary deficit and R_t^r is bigger than y_t. Therefore, sustaining debt requires the opposite; R_t^r must be smaller than y_t.

Employing this strategy comes with both positive and negative effects. In their analysis, Marattin, Marzo, and Zagaglia (2011) found that productive government expenditure contributes more to welfare as oppose to increased tax for the Economic and Monetary Union (EMU) of Europe. In the case of South Africa, this strategy leads to improvements in deficit to GDP ratio as well as long term GDP (Mabugu et al., 2013). However, the study done by Teles and Mussolini (2014) points to the opposite. The study shows that the effect of productive expenditure on long term growth is constrained in the event of high public debt to GDP ratio. Sutherland (1997) had reached to similar conclusion.

On the other hand, NC economics believes that government should increase tax to mitigate high public debt. Courtault and Magnani (2012) simulated various scenarios to see whether European countries can attain debt sustainability through taxable distributable surplus and conclude that France, Germany, and the United Kingdom are able to sustain their debt. Studying the case of Japan, Hansen and İmrohoroğlu (2016) found that the targeted debt to GDP ratio of 60% can be attained by increasing consumption tax rates. In fact, Sakuragawa and Hosono (2011) agreed with this as their findings also shows that Japan need to have a primary surplus to attain debt stabilisation. Qin, Cagas, Ducanes, Magtibay-Ramos and Quising (2006) also proposed increase in tax rates to combat rising debt of the Philippines. For the case of Brazil, Tourinho et al. (2013) recommended an increase in primary surplus roughly around 3.11% of GDP to sustain the Brazilian debt to GDP of 40.35%.

Still, this strategy often has undesirable consequences. Firstly, there is evidence that shows an increase in budget deficit instead where output is already dropping by 30% and inflation by 2% (Denes, Eggertsson, & Gilbukh, 2012). Secondly, this strategy negatively impacts welfare. This impact on welfare is the most major critic that NC economics face. Marattin et al. (2011) studied different means to sustain debt in the wake of the European sovereign debt crisis of 2008 and found that increasing capital income taxation rates minimises welfare the most.

Zieliński (2014) proposed that the government should reduce interest rate to channel in cheap funding. Low interest rate results in a lower debt burden (Çebi, 2012). At the same time, the resulting inflation will increase the growth of GDP at a faster rate and further lessen the burden of government debt as interest rate becomes negative. Similarly, a simulation done by Leith and Wren-Lewis (2008) showed that a sudden inflation is needed to result in stationary debt in the case where debt to GDP ratio is more than 30%. Despite this, there are several implications of high inflation including riskier debt composition and deterring government from issuing credible long-term bonds (Mehl & Reynaud, 2010).

Some studies showed proof of sustained debt through a combination of strategies. Baldacci and Mulas-Granados (2015) concluded that increase in tax while maintaining public investment (which is part of government expenditure) contributes to reduction in public debt as well as maximizing medium term growth. This result is based on countries where credit is restricted and discretionary fiscal policy is employed to reduce public debt. Meanwhile, Cogan, Taylor, Wieland, and Wolters (2013) tested the United States (US) economy in the event that tax as well as expenditure are gradually decreased. Their findings state that as tax decreases, GDP and employment improves while the decrease

in expenditure makes it possible for the US government to save and use that savings to pay outstanding debt.

Another mixture of strategies is to increase tax while reducing government expenditure which is widely termed as an austerity measure. Konzelmann (2014) discussed in-depth about the evolution of austerity economics as well as austerity measures and cited many evidences against austerity. These include contractionary fiscal consolidation, lower tax collection, and higher debt to GDP ratio. There is also the possibility of mixing strategies between periods. Rieth (2014) suggested the introduction of soft borrowing constraint in the long term because debt tend to build up by then. The researcher defined soft borrowing constraint as a debt threshold of which the government can only borrow up until a certain amount, thus, preventing debt from accumulating. In particular, the government incurs debt as oppose to increase tax in the short term and government increases tax to finance for the cost of debt in the medium term.

There is scarce literature on the study of debt management strategy from Islamic economics. This is largely because in an ideal Islamic economics, public debt should not be high. There are three reasons for this claim (Metwally, 1983). First, since charging interest rate is not permissible in Islam, the government does not need to service debt. Second, should the maturity date be postponed, the value of government debt stays the same since there is no charge whatsoever. Third, as the public debt is little, there is no need for the government to target for a frequent budget surplus. This study obviously contradicts reality because current Muslim economies are borrowing with interest and are experiencing public debt problems.

Metwally (1983) further postulated that fiscal policy in an Islamic economy is more likely to increase expenditure and revenue equally. So, if there is a debt strategy by Muslims, then the debt strategy must be tied in with the said fiscal policy. This is strongly

supported by Muhammed Ibn Khaldun (1377) who claimed that the lifestyles of Muslim states were not luxurious at first; hence, revenue can cover expenses and budget surplus was a frequent occurrence. Still, there are also evidences that point towards the use of productive expenditure. Muhammed Ibn Khaldun (1377) in his monumental work described how the Muslim government in history imposed low tax rates which gave motivation to more persons to engage in business. As a result, collection of tax increased. However, as the government became luxurious, tax rates became higher. In turn, persons were dissuaded from doing business because their after-tax profit became low. The end result was a reduction in tax collection.

Indeed, studies on government debt strategy from the Islamic economics perspective are mostly regressive simply because there should never be issue of debt instability in the Islamic world. To be critical, most of the studies do not practically answer the dilemma of modern Muslim countries that has the tendency to incur interest. Since solutions to government debt problem is saturated from the conventional perspective, it is perhaps wise to emulate certain conventional strategies without compromising Islamic principles. Adi (2014) approves of this. Aside from the prohibition of interest, Islamic economics must always guarantee welfare. This is in line with Chapra (1992); two out of the five objectives in the Islamic economics order are to ensure economic well-being which also guarantees a decent standard of living. In other words, reducing government expenditure and increasing tax are unfavourable options.

Referring back to Equations 1.0 and 1.1, it is easy to observe that increased GDP growth and/or reduced interest rate are the only two options left. However close inspection of the equations show that only public and private sector variables are taken into account while third sector variable is virtually non-existent. It indicates a lacking third sector interaction in the public finance sphere. This should not be the case because

79

Abu-Rashed and Belarbi (1993) had mathematically showed the contributions of altruistic behaviour in conventional economic theory and Pestoff (1992) outlined how the third sector interact within the European economy. Furthermore, the development of Malaysian framework for *waqf* (Figure 2.8 in Section 2.5) served as another evidence for the role of *waqf* in Malaysian economic setting. Thus by extension of these studies and Figure 2.8, there are probable cause for *waqf* to be included in Equation 1.0.

It has already been deliberated in Section 2.3.1 that *waqf* had been financing public goods and other social services in history. At present, these items are the major responsibilities of the government. Therefore, if *waqf* were to cater these items, then the government can steadily decrease its spending on these items which ultimately reduces federal government debt. Similar strategy was proposed by Çizakça (1998). On top of that, welfare is not jeopardised because the reduction in government spending is supplemented by *waqf*. Of course, this is only in theory and further proofs are needed.

3.6   Techniques to Evaluate the Burden of Government Debt

Now that the strategies to sustain government debt problem are known, it is only natural to know the procedures to evaluate the state of government debt and give precedence to RO 3. To the knowledge of this researcher, there is little or no research that uses mathematical methods to study the impact of *waqf* on government debt. Hence, selection of method is vital for this thesis.

The basis for determining whether debt is sustainable or not is to check for the No Ponzi Game (NPG) condition on the government's budget constraint (Equation 1.1). According to Azizi, Canry, Chatelain, and Tinel (2012), NPG condition states that "the growth of private debt and of public debt has to be lower than the real interest rate charged

on this debt in the very long run" (p.4). Neck and Sturm (2008) explains this in a simpler manner; governments just cannot issue new debt to pay for older debt and interest. Thus, mathematically, the total discounted value of all future debts must equal to zero. This can be determined by testing the (1) null unit root hypothesis or (2) no cointegration between government spending and revenue, the two basic econometric analyses (Uctum M., Thurston, & Uctum R., 2006; Qin et al., 2006; Fincke & Greiner, 2010; Adams, Ferrarini, & Park, 2010). Checcherita and Rother (2010) and Baldacci and Mulas-Granados (2015) had also conducted econometric analysis but through the use of panel data.

Now Uctum M. et al. (2006) showed that results from checking for NPG is doubtful in countries that had experienced structural breaks. Hence, Uctum M. et al. (2006) had proposed the reaction function approach which tests the relationship between the primary surplus and the level of government debt. Still, the econometric techniques and the reaction function approach do not take into account the data on *waqf*. Although *waqf* variable can be inserted and econometric analysis performed, one must understand that *waqf* is endowed voluntarily. Thus, it requires another equation that models the *waqif*'s behaviour.

In another study conducted by Dumitrescu (2014), primary budget gap method was applied instead. Primary budget gap is the difference between the sustainable value of primary balance and the forecasted primary balance value. Positive primary budget gap indicates unsustainability of public debt and vice versa. This method is also not appropriate for the same reason of which the *waqif*'s behaviour is not incorporated.

Essentially, the study of debt sustainability is associated with other markets in the economy. Macroeconomic general equilibrium (GE) model studies the interaction between different markets through a system of equations in a GE economy. The GE occurs precisely "when prices have fully adjusted so that supply equals demand in all

markets" (Starr, 2011, p.5). The GE is a theory that was first formally introduced by Léon Walras in 1874 and culminated in its mathematical proof by Gerard Debreu and Herbert Scarf in 1963 (Starr, 2011).

Structure of that mathematical proof combined with real economic data ushered in a simulation technique that can mathematically solve the levels of demand, supply, and price at equilibrium across all specified markets. This simulation technique is called computable GE (CGE) model (Wing, 2012). It was Leif Johansen that had formally developed the first CGE model in 1960 by specifying the behaviour of individual economic agents (Dixon & Rimmer, 2010) when precursor models focused on markets as a whole. As such, CGE model can also be argued as a microfounded model that addresses the Lucas critique. Later on, Kydland and Prescott (1982) fully established the dynamic stochastic GE (DSGE) model. DSGE model basically retains the specification of individual economic agents as in CGE model. However, DSGE model is a dynamic model and allows for stochastic equation. Thus dynamic GE (DGE) model, another strand of macroeconomic GE model, does not contain any stochastic equations.

Whether it be macroeconomic GE model, DGE model, CGE model, or DSGE model, the theoretical model employed in these methods should represent a simplified version of reality and can give valid economic facts. This can be assured by employing theoretical models from different school of economic thoughts as a basis. For instance, Leith and Wren-Lewis (2008), Marattin et al. (2011), Çebi (2012), Denes et al. (2012), Tourinho et al. (2013), as well as Cogan et al. (2013) used a standard NK model. Sakuragawa and Hosono (2011) adopted the Real Business Cycle (RBC) model instead. Meanwhile, Courtault and Magnani (2012), Mabugu et al. (2013), Teles and Mussolini (2014), as well as Hansen and İmrohoroğlu (2016) employed the standard Neoclassical model in their debt sustainability studies. Rieth (2014) also employed the same albeit loosely. These

studies excluding Courtault and Magnani (2012) have three economic agents which are households, firms, and government which is similarly shown in Figure 2.8. Therefore, Neoclassical model should be a good fit for this thesis so far.

Now, CGE model and DSGE model are two suitable methods to study the impact of *waqf* financing on debt because both methods are contemporary and can specify the behaviour of *waqif*. However, CGE model is often criticised as "a "black box" whose results cannot be meaningfully traced to any particular features of their data base or input parameters, algebraic structure, or method of solution" (Wing, 2004, p.2). In other words, discussing the results of the impact of *waqf* financing on debt in a meaningful manner may be problematic. Furthermore, DSGE model is a dynamic model, hence, highly imitates the dynamic nature of the real economy while allowing random statistics.

Besides, DSGE model is frequently used more than CGE model in the study of debt economics. Sakuragawa and Hosono (2011), Çebi (2012), Denes et al. (2012), Cogan et al. (2013), and Tourinho et al. (2013) employed DSGE model while Courtault and Magnani (2012) as well as Mabugu et al. (2013) employed CGE model. On a side note, Leith and Wren-Lewis (2008), Marattin et al. (2011), Teles and Mussolini (2014), Rieth (2014), as well as Hansen and İmrohoroğlu (2016) applied macroeconomic GE model instead. Although this also shows that more studies on debt employed macroeconomic GE model, DSGE model is more modern. Plus, fewer studies on debt using DSGE model means that this thesis can add more to its literature. These arguments further cement the use of DSGE model in this thesis.

Lesser used debt sustainability methods are as follows. Sutherland (1997) employed a simple macroeconomic model that consist of equations for household and government behaviour. Definition for *waqf* in economics stated by Kahf (2014) calls for investment to which Sutherland (1997) did not consider. Meanwhile, Sopek (2011) tested the public

debt sustainability of Croatia in pessimistic, baseline, and optimistic scenarios using stress tests. In stress test, variables in different scenarios are given shocks to see the deviations that these variables make. Still, these shocks can also be introduced in a DSGE model. Socol (2013) used a toolkit developed by the World Bank that is based on three inputs; macroeconomic, budgetary, and variables related to public debt. Monte Carlo simulation were then employed to assess the risk of Romania's public debt. Since the World Bank toolkit does not include the *waqf* variable, this method would not be able to answer RO 3.

Lastly, institutions like Development Finance International (DFI) and the International Organization of Supreme Audit Institutions (INTOSAI) had summarised a set of indicators that can be used to assess the sustainability of debt such as debt to GDP ratio, debt service to exports, present value of debt to exports, and myriad others (DFI, 2008; INTOSAI, 2010). These indicators are highly unsuitable for this thesis because the *waqf* variable cannot be factored in and are static in nature.

3.7   The Resulting Conceptual Framework

Contingent on the literature review covered in Chapter 2 and Chapter 3, the guiding conceptual framework of this thesis is encapsulated in Figure 3.10 below:
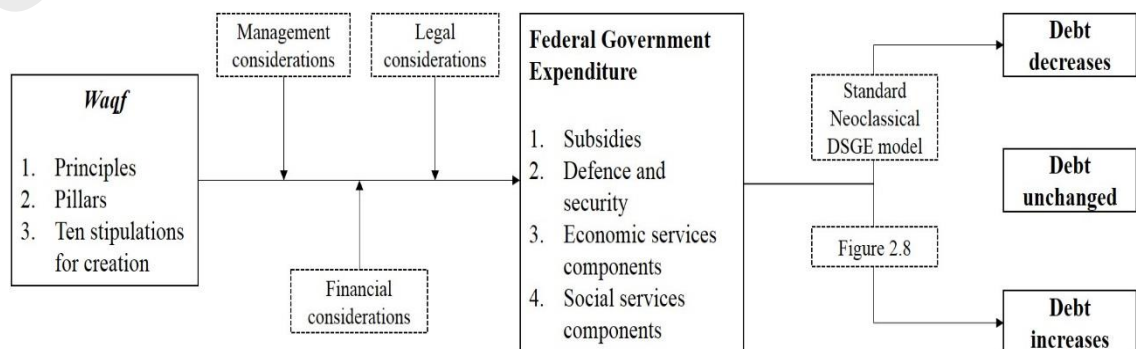
Figure 3.10: The Conceptual Framework

The principles, pillars, and ten stipulations for creation of waqf are the key elements that define *waqf*. To reiterate, *waqf* has three chief principles which are perpetuity, irrevocability, and inalienability. However, Section 2.2.1 also mentioned that temporary *waqf* is valid in the Maliki madhab and perpetuity is emphasised more on the benefits as opposed to the capital of *waqf*. Meanwhile, the pillars of *waqf* are *waqif*, *mawquf*, *mawquf 'alaih*, *sighah,* and *mutawalli*. These have been listed in Section 2.2.2. Lastly, the ten stipulations for *waqf* creation or five pairs of stipulations for *waqf* creation were outlined in Section 2.2.3, namely *ziyadah* and *nuqsan*, *idkal* and *ikhraj*, *i'ta'* and *hirman*, *taghyir* and *tabdil*, as well as *istibdal* and *ibdal*.

In order for *waqf* to be able to finance federal government expenditure, this thesis have to take into account the legal considerations, management considerations, and financial considerations of Malaysian *waqf*. These were discussed at length in Section 2.4.1 to Section 2.4.3. The components of federal government expenditure that are suitable for *waqf* are subsidies, defence and security, economic services component, and social services component. Arguments for these are contained in Section 3.2. The fact that *waqf* can finance these expenditures are mainly due to its application in the past (Section 2.3.1).

To investigate the impact of this *waqf* application on debt, standard Neoclassical DSGE model is employed. The result from this model thus addresses RO3. Reasons for the use of said model were elaborated in Section 3.6. To recapitulate, the DSGE model is the most modern method for debt sustainability studies and provides platform for *waqf* interactions with other economic agents. Meanwhile, Neoclassical theory is considered because it coincides with the economic agents in Figure 2.8.

3.8   Conclusion

This chapter had identified the components of Malaysian federal government expenditure that are suitable for *waqf* endowments which are subsidies and all the components of development expenditure except for general administration. The chapter then demonstrated the increasing debt to GDP ratio and the persistent primary deficit to which *waqf* can help mitigate by financing certain federal government expenditure components. The dangers of excessive debt were further emphasised in the conventional economic schools of thought while indicative in the Islamic schools of thought. Naturally, methods to sustain and evaluate debt were then reviewed to which two important points emerged. First, the DSGE model is the most suitable method to study the impact of *waqf* on debt. Second, a significant bulk of the literature never took into account any third sector component such as *waqf* in evaluating the performance of debt. These points address a large gap on *waqf* in the public finance sphere, hence, giving much weight to the significance of this thesis. Lastly, a conceptual framework was developed by summarising the literature review done in this chapter with that of Chapter 2.

CHAPTER 4: DATA AND METHODOLOGY

4.1 Introduction

To attain the objectives of this thesis, this researcher must answer the RQs through a systematic and rigorous research process. Analysis of RQ 1 to RQ 3 are performed qualitatively to fulfil RO 1 and RO 2. In addition to that, findings from RO 2 will supply data for the implementation of quantitative analysis to fulfil RO 3. Thus, Chapter 4 is dedicated to explaining the research methodology employed by this thesis to answer the ROs and RQs.

Basically, this chapter is organised as follows. Section 4.2 argues the research methodology chosen for this research. Section 4.3 outlines the research design of choice. Section 4.4 states the conceptual framework that governs the overall thesis. Section 4.5 presents the theoretical framework to which the quantitative component is built upon. By extension, the theoretical model and hypothesis of the quantitative study is also explained. Section 4.6 details on the research strategy. Section 4.7 states the research methods used to collect qualitative and quantitative data. Section 4.8 describes the data analysis techniques that are opted for this thesis. Lastly, Section 4.9 concludes this chapter.

4.2 Research Methodology

Research methodology constitutes practical stages or steps in the course of research so as to find the answers to research questions (Kumar, 2011). These practical steps must also be rationalised throughout. On the other hand, research methods are the techniques undertaken to conduct research (Walliman, 2011). Therefore, research methodology has a wider connotation than research methods.

87

This thesis employs mixed methods research. As mentioned in Creswell (2010), Johnson, Onwuegbuzie, and Turner (2007) defined mixed methods research as "the type of research in which a researcher or team of researchers combines elements of qualitative and quantitative research approaches (e.g., use of qualitative and quantitative viewpoints, data collection, analysis, inference techniques) for the purposes of breadth and depth of understanding and corroboration" (p.51). The philosophical underpinning of mixed methods research is the pragmatic knowledge school of thought (Creswell, 2003). This school of thought believes that the problem of interest is more important than the research method, hence, researchers will opt for plural approaches to understand the problem in order to solve it. Thus, opting for mixed methods research gives this researcher the freedom to use both qualitative and quantitative methods to provide coherence and comprehensive findings.

To be specific, *waqf* financing public goods and social services were only significantly implemented in the past. On the other hand, this thesis attempts to investigate the case where these goods are financed by government expenditure in the present Malaysian economic setting. Hence, a qualitative approach to research which are exploratory in nature is the best approach to acquire understanding on this matter. In terms of determining the effect it has on government debt, results obtained from qualitative research is not sufficient. More precise evidence must be obtained through an explanatory approach instead. Plus, based on the literature, studies on government debt burden is often done quantitatively. To evaluate debt quantitatively, a theoretical model must first be built which requires certain information that can only be acquired through qualitative approaches. This information is the form of *mawquf* that is best and how to ensure that the *mawquf* remains perpetual. Therefore, employing mixed methods research better answer the ROs of this thesis which is in itself, a major advantage.

As with other research methodology, mixed methods research has its weakness too. The major drawback is that the research period becomes longer. As this thesis adopts exploratory sequential design (refer to Section 4.3), qualitative data collection and analysis should be performed first. Thus, any delay in the qualitative part would further delay the undertaking of the quantitative part. The delay can happen in the form of getting interview appointments, transcribing interview transcripts, and others. Regardless, the advantage of mixed methods research far outweighs this disadvantage as explained earlier.

4.3 Research Design

This thesis adopts the exploratory sequential design. Exploratory sequential design begins by collecting and analysing qualitative data. Results from qualitative analysis will then inform the quantitative component. Information from qualitative results will then be used to collect relevant quantitative data before analysing. Lastly, results from both qualitative and quantitative are mixed and interpreted. The design can be seen in Figure 4.1.

Qualitative Data Collection and Analysis	Builds to	Quantitative Data Collection and Analysis	Interpretation
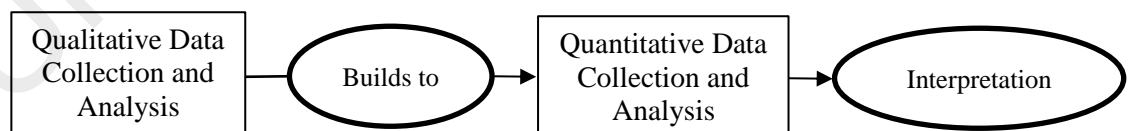
Figure 4.1: The Exploratory Sequential Design

Source: Creswell and Clark (2006, p.69)

Specific for this study, the qualitative component is needed to thoroughly understand the viability of *waqf* financing public expenditures and issues that may arise in the

Malaysian setting (RO 1). As a result, recommendations can be made to come out with a model of *waqf* financing public expenditures and a complete theoretical model can be developed using the qualitative data (RO 2). In the process, opinions from experts are also gathered and quantitative analysis performed to investigate the impact of that *waqf* application on debt (RO 3). Result from the quantitative analysis will confirm or reject the interviewees' opinions on the impact that the *waqf* has on debt. This adds depth to the findings of RO 3. Finally, this researcher will consolidate the findings from both the qualitative and quantitative components to add rigour to this thesis.

4.4   Conceptual Framework

The conceptual framework stems from the literature gaps which subsequently relate to the ROs. It guides the overall research process and has already been elaborated at length in Section 3.7. Since the conceptual framework is quite often provided in the data and methodology chapter, as well as for convenience purposes, it is recapitulated below as Figure 4.2:
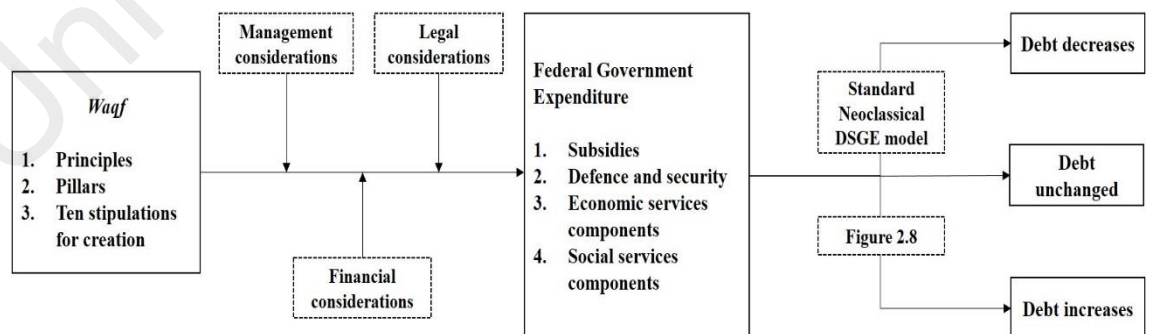
Figure 4.2: The Conceptual Framework

4.5   Theoretical Framework

The theoretical framework is vital for the quantitative part of this study. Theoretical framework is a mandatory component for a quantitative research process. It consists of a theory, or several theories, that governs the research and acts as a foundation for quantitative studies.

The theory used in the quantitative part of this study is the GE theory that was first formally introduced by Léon Walras in 1874. To reiterate, GE Theory states that there exist a set of prices across all markets that will result in an overall economic equilibrium and these prices are in equilibrium when demand equals supply in each of these markets (Debreu, 1983; Cardenete, Guerra, & Sancho, 2012). This theory has greatly facilitated the building of different forms of macroeconomic model to study various policy implications. Hence, this theory is the basis for the study of *waqf* financing public expenditures on government debt.

4.5.1   Theoretical Model

Torres (2013) defines theoretical model as "abstract assumptions which represents a simplification of reality, but the important thing is that they can be useful to offer a valid explanation of an economic fact" (p.6). Based on the conceptual framework, a standard Neoclassical theoretical model depicting a closed economy fits best. To recapitulate, studies that employ Neoclassical model such as Mabugu et al. (2013), Teles and Mussolini (2014), Rieth (2014), as well as Hansen and İmrohoroğlu (2016) have three economic agents which are households, firms, and the government which coincides with Figure 2.8. Besides, analysis that is based on Neoclassical economics begins with the behaviour of households (Tsoulfidis, 2010) which in the context of this thesis, can be

modelled as altruistic. As a consequence of their altruism, households are willing to endow *waqf*.

The forming of theoretical model for this thesis however, require results from qualitative analysis, hence, only an incomplete form is presented in Section 4.5.1.1 to Section 4.5.1.4. This is because information on the form of *mawquf* and how to guarantee the *mawquf*'s perpetuity are needed to complete the theoretical model. The following is based on a simple theoretical model developed by Torres (2013) consisting of only two agents, household and firm but for the case of this thesis, modified to incorporate government and altruistic behaviour of households. Meanwhile, the behaviour of government is an alteration from Galí, López-Salido, and Vallés (2007) and is also modified to include usufruct from *waqf* endowment. To clarify, the general term "usufruct" is used intentionally because the form of *mawquf* and manner to ensure that *mawquf*'s perpetuity has not yet been figured out at this point.

4.5.1.1 Households

The economy consists of many households where each make economic decisions. In order to analyse only one economic decision, the concept of a representative household agent is employed. We assume further that all agents have similar preference. Two functions to be defined for household is the utility function and budget constraint.

Households decide on total consumption, C_t^τ, and leisure, O_t, that are subjected to a budget constraint in order to attain utility or happiness. Total consumption is the amount of goods and services consumed by the representative agent while leisure is the remaining time left after labour services (L_t). Due to the altruistic behaviour of the representative

agent, *waqf* contribution essentially becomes part of his consumption. Hence C_t^τ can be broken down into consumption (C_t) and *waqf* contribution (V_t):

$$C_t^\tau = C_t + V_t \tag{1.2}$$

It is also important to state that total available discretionary time is normalised to 1 and leisure is total available discretionary time minus labour services or working time. This means that equation containing O_t and L_t can be written as follows:

$$O_t + L_t = 1$$

$$O_t = 1 - L_t \tag{1.3}$$

As was mentioned, the utility of the representative agent is constraint by a budget. The representative household are the owner of productive factors namely capital, K_t and labour, L_t. By renting these productive factors to firms, the representative agent receives R_t which is the return for K_t and wage, W_t as return for his L_t. After paying for tax, T_t, earnings from the household agent is spent on C_t and V_t while the remaining is put into savings, S_t. We assume further that due to a competitive sector, S_t is directly transform into investment, I_t and federal government bonds, B_t without any cost thus:

$$S_t = B_t + I_t \tag{1.4}$$

The agent receives a return of R_t^r from purchasing past bonds B_{t-1} while I_t follows a process of capital accumulation overtime following a simple inventory accumulation equation:

$$I_t = K_{t+1} - (1 - \delta)K_t \tag{1.5}$$

Although Equation 1.5 is theoretically correct, capital is actually decided yesterday making capital a predetermined variable. This transforms Equation 1.5 into Equation 1.6:

$$I_t = K_t - (1 - \delta)K_{t-1} \tag{1.6}$$

Therefore, the intertemporal maximisation problem of the representative household agent is given as:

$$\max E_t \sum_{t=0}^{\infty} \beta^t U[C_t, O_t, V_t] \tag{1.7}$$

such that

$$C_t + V_t + S_t = W_t L_t + R_t K_{t-1} + B_{t-1}(1 + R_t^r) - T_t \tag{1.8}$$

Equation 1.7 is the utility function of the representative household where β, $\beta \in (0,1)$ is the intertemporal discount factor which specifies how much the agent values his/her future utility as oppose to his/her current utility. Meanwhile, Equation 1.8 is the household's budget constraint.

To facilitate simple calculation, the utility function can be expressed in a log linear form. Further substituting Equation 1.3 into Equation 1.7 as well as Equation 1.4 and Equation 1.6 into Equation 1.8:

$$\max \ E_t \sum_{t=0}^{\infty} \beta^t [\mu \log C_t + \gamma \log(1 - L_t) + \eta \log V_t] \tag{1.9}$$

such that

$$C_t + V_t + K_t - (1 - \delta)K_{t-1} + B_t = W_t L_t + R_t K_{t-1} + B_{t-1}(1 + R_t^r) - T_t \tag{2.0}$$

μ, γ, and ν are the preference parameter for C_t, $1 - L_t$, and V_t respectively where $\mu + \gamma + \eta \approx 1$. Specifically, μ represents the proportion of consumer spending to total

income, γ represents the proportion of leisure to total income, and ɳ represents the proportion of *waqf* endowment to total income. In economic terms, μ can also be defined as the marginal propensity to consume, γ as the marginal propensity to leisure, and ɳ as the marginal propensity to endow *waqf*. Basically, these preference parameters indicate the agent's preferences toward consumption – leisure – *waqf* endowment decisions.

Household will want to maximise C_t, V_t, L_t, K_t, and B_t. This household problem can be solve using dynamic Lagrangian calculation before deriving first order conditions (FOCs):

$$\mathcal{L} = \sum_{t=0}^{\infty} \beta^t \left[\begin{array}{c} \mu \log C_t + \gamma log(1 - L_t) + v \log V_t \\ \\ \\ - \lambda_t[C_t + V_t + K_t - (1 - \delta)K_{t-1} + B_t - W_t L_t - R_t K_{t-1} - B_{t-1}(1 + R_t^r) + T_t] \end{array} \right]$$

λ_t is the Lagrange multiplier of period *t*. As the capital for a given period appears in time *t-1* and in time *t*, the restriction faced by households at time *t* is:

$$\dots - \beta^t \lambda_t[C_t + V_t + K_t - (1 - \delta)K_{t-1} + B_t - W_t L_t - R_t K_{t-1} - B_{t-1}(1 +$$

$$R_t^r) + T_t] - \beta^{t+1}\lambda_{t+1}[C_{t+1} + V_{t+1} + K_{t+1} - (1 - \delta)K_t + B_{t+1} - W_{t+1}L_{t+1} - R_{t+1}K_t -$$

$$B_t(1 + R_{t+1}^r) + T_{t+1}] \tag{2.1}$$

The first order conditions (FOCs) of the household problem are:

$$\frac{\partial \mathcal{L}}{\partial C} = \beta^t \left[\frac{\mu}{C_t} - \lambda_t \right] = 0$$

$$\lambda_t = \frac{\mu}{C_t} \tag{2.2}$$

$$\frac{\partial \mathcal{L}}{\partial L} = \beta^t \left[\frac{\gamma}{1 - L_t}(-1) + \lambda_t W_t \right] = 0$$

$$\lambda_t W_t = \frac{\gamma}{1 - L_t} \tag{2.3}$$

$$\frac{\partial \mathcal{L}}{\partial V} = \beta^t \left[\frac{\eta}{V_t} - \lambda_t \right] = 0$$

$$\lambda_t = \frac{\eta}{V_t} \tag{2.4}$$

$$\frac{\partial \mathcal{L}}{\partial K} = -\beta^t \lambda_t + \beta^{t+1} \lambda_{t+1} [R_{t+1} + 1 - \delta] = 0$$

$$\beta^t \lambda_t = \beta^{t+1} \lambda_{t+1} [R_{t+1} + 1 - \delta]$$

$$\frac{\lambda_t}{\lambda_{t+1}} = \beta [R_{t+1} + 1 - \delta] \tag{2.5}$$

$$\frac{\partial \mathcal{L}}{\partial B} = -\beta^t \lambda_t + \beta^{t+1} \lambda_{t+1} [1 + R_{t+1}^r] = 0$$

$$\beta^t \lambda_t = \beta^{t+1} \lambda_{t+1} [1 + R_{t+1}^r]$$

$$\frac{\lambda_t}{\lambda_{t+1}} = \beta [1 + R_{t+1}^r] \tag{2.6}$$

By equating equations (2.2) and (2.4) we obtain:

$$V_t = \frac{\eta}{\mu} C_t \tag{2.7}$$

Equation (2.7) determines the agent's decision between endowing *waqf* or consuming. Basically, the right hand side of equation (2.7) is the opportunity cost of endowing an additional unit of *waqf*. Substituting equation (2.2) into (2.3) we obtain:

$$W_t = \frac{\gamma C_t}{\mu(1 - L_t)} \tag{2.8}$$

Equation (2.8) equates the marginal rate of substitution between consumption and leisure

$\left(\frac{\gamma}{\mu}\right)$ to the opportunity cost of an additional unit of leisure (W_t). Another way to view W_t

is to substitute equation (2.4) into (2.3) instead:

$$W_t = \frac{\gamma V_t}{\eta(1 - L_t)} \tag{2.9}$$

Equation (2.9) equates the marginal rate of substitution between endowing *waqf* and

leisure to the opportunity cost of an additional unit of leisure.

From (2.2) we get:

$$\lambda_{t+1} = \frac{\mu}{C_{t+1}} \tag{3.0}$$

Substituting Equation 3.0 and Equation 2.2 into Equation 2.5 and Equation 2.6:

$$\frac{C_{t+1}}{C_t} = \beta[R_{t+1} + 1 - \delta] \tag{3.1}$$

$$\frac{C_{t+1}}{C_t} = \beta[1 + R_{t+1}^r] \tag{3.2}$$

Equation 3.1 defines the condition of the agent's decision about investment. Basically,

the agent compares the utility of consumption with that of investment. On the other hand,

Equation 3.2 indicate that the agent compares the utility of consumption with that of

purchasing bonds.

4.5.1.2 Firms

Firms rent L_t and K_t from households. These production factors are then converted

into final goods (Y_t). Firms then pay labour $W_t L_t$ and $R_t K_{t-1}$ to households. Since the

sole owners of production factors are the households, firms do not make investment

decision nor decide on the amount of hired inputs from period to period. This is to

simplify the theoretical model following Torres (2013). It causes the maximization problem of the firm to become a static equation:

$$\pi = Y_t - W_t L_t - R_t K_{t-1} \tag{3.3}$$

Y_t also follows a Cobb-Douglas production function and has constant returns to scale whereby

$$Y_t = A_t F(K_{t-1}, L_t) = A_t K_{t-1}^{\alpha} L_t^{1-\alpha}$$

A_t is the technology or total factor productivity. Following Gali et al. (2007), we normalize A_t to unity and Y_t becomes:

$$Y_t = A_t K_{t-1}^{\alpha} L_t^{1-\alpha} \tag{3.4}$$

α is the output elasticity of K_t. The firm's maximization problem thus becomes:

$$\pi = K_{t-1}^{\alpha} L_t^{1-\alpha} - W_t L_t - R_t K_{t-1} \tag{3.5}$$

The firm maximises profit by choosing labour and capital. To solve the firm's problem, we take FOCs:

$$\frac{\partial \pi}{\partial L} = (1-\alpha) K_{t-1}^{\alpha} L_t^{-\alpha} - W_t = 0$$

$$W_t = (1-\alpha) K_{t-1}^{\alpha} L_t^{-\alpha} \tag{3.6}$$

$$\frac{\partial \pi}{\partial K} = \alpha K_{t-1}^{\alpha-1} L_t^{1-\alpha} - R_t = 0$$

$$R_t = \alpha K_{t-1}^{\alpha-1} L_t^{1-\alpha} \tag{3.7}$$

Substituting Equation 3.4 into Equation 3.6 and 3.7 we respectively obtain:

$$W_t = (1 - \alpha) \frac{Y_t}{L_t} \tag{3.8}$$

$$R_t = \frac{\alpha Y_t}{K_t} \tag{3.9}$$

Equation 3.8 shows the wage rate that the firm is willing to pay the household which is a proportion of the total output over labour. On the other hand, Equation 3.9 indicates that the rental rate is a proportion of the total output over capital.

4.5.1.3   Federal government

The federal government budget constraint is given as:

$$B_t = B_{t-1}(1 + R_t^r) + G_t - T_t - V_t D_t \tag{4.0}$$

The government borrows B_t when T_t and value of usufruct from *waqf*, $V_t D_t$ are insufficient to finance for total federal government expenditures, G_t (i.e. sum of federal government operating and development expenditure), federal government debt B_{t-1}, and interest on that debt (R_t^r). Hence Equation (4.0) states that bond financing is employed to finance expenditure, service debt, and when usufruct from *waqf* is insufficient to finance the selected public expenditures. It is the federal government's responsibility as a *mutawalli* to spend the usufruct of *waqf* on specified public expenditures only.

Let $\hat{S}_t = T_t - G_t$ and dividing Equation (4.0) by Y_t:

$$b_t = b_{t-1}(1 + R_t^r) - \hat{s}_t - v_t D_t \tag{4.1}$$

whereby

$$b_t = \frac{B_t}{Y_t} \tag{4.2}$$

$$v_t = \frac{V_t}{Y_t} \tag{4.3}$$

$$ŝ_t = \frac{Ŝ_t}{Y_t} \tag{4.4}$$

The fiscal policy rule that determines the primary balance-to-GDP ratio, $ŝ_t$ is specified as:

$$ŝ_t = \theta_0 \bar{\bar{s}} + \theta_1 ŝ_{t-1} + \theta_2 D_t + e_1 \tag{4.5}$$

whereby $\theta_0 = 1 - \theta_1 - \theta_2$ and $\bar{\bar{s}}$ is the steady state value of primary balance-to-GDP ratio. This manner of specification mimics Sakuragawa and Hosono (2011) and Torres (2013). Equation 4.5 simply states that the current primary balance-to-GDP ratio is determined by its steady state value (ŝ), its past value, and the current rate of usufruct from *waqf*, D_t. The insertion of D_t in Equation 4.3 captures the excess income from *waqf*.

4.5.1.4 Market Clearing

The feasibility constraint in the economy can be stated as:

$$Y_t = C_t + V_t + I_t + G_t \tag{4.6}$$

whereby

$$G_t = g_t Y_t \tag{4.7}$$

g_t is simply G_t over Y_t or total federal government expenditure over GDP. It follows a first order autoregressive (AR(1)) process:

$$g_t = (1 - \varphi)\bar{g} + \varphi g_{t-1} + e_2 \tag{4.8}$$

whereby $\bar{g}$ is the steady state value of g. This form of specification follows Torres (2013).

4.5.2   Hypothesis of the Study

Testing of hypothesis helps this study to fulfil its objectives. Hypothesis is "a tentative explanation that accounts for a set of facts and can be tested by further investigation" (Muijs, 2004, p.8). Further investigation involves the analysis of data after which the researcher should either reject or accept the null hypothesis, H_0. Take note that qualitative research which is another component of this study do not require hypothesis testing. Below are the hypotheses for this study:

H_0: Federal government debt to GDP ratio declines when *waqf* finances certain federal government expenditure components.

H_1: Federal government debt to GDP ratio does not decline when *waqf* finances certain federal government expenditure components.

4.6   Research Strategy

Research strategy simply means the overall plan opted by the researcher in answering the research questions of a given study. Mixed methods research has three types of research strategy which are (1) sequential, (2) concurrent, and (3) transformative (Creswell, 2003). Since this study employs exploratory sequential design, it is only obvious that this research's strategy is sequential mixed methods. Conducted in sequence, qualitative data was collected first to inform the quantitative phase of this research. The qualitative phase was needed to inform the quantitative phase on the form of *mawquf* that

is suitable for implementation and how to ensure the perpetuity of that *mawquf*. In addition, the qualitative phase also provided confirmation on the result obtained from the quantitative phase. Meanwhile, the integration of both the qualitative and quantitative findings help produced comprehensive results for this thesis.

4.7   Data Collection

Collecting data is an instrumental part of any research which is then used for data analysis to produce findings. In this thesis, both primary data and secondary data were collected. Section 4.7.1 and Section 4.7.2 further details on the various aspects of data collection.

4.7.1   Qualitative Method: Semi-Structured Interview

Semi-structured interview involves initial preparation of interview questions by the interviewer and at the same time, grants the interviewer the flexibility to add, delete, or alter questions (Carley-Baxter, 2008). The interview guidelines for this thesis were prepared based on the conceptual framework and stated as follows:

1. In past Muslim economies, public goods and mixed public goods were financed by *waqf*. Can the same be applied in the present Malaysian context and why is that so?

2. As is now typical in modern economy, public goods and mixed public goods are part of the Malaysian federal government expenditures. Knowing this, can *waqf* finance these expenditures?

3. In your opinion, do *waqf* have a role in the public finance field? If yes, how exactly?

4. What are issues that can impede the use of *waqf* to finance public goods and mixed public goods?

5. How is *waqf* currently administered in Malaysia and will this current administration impede *waqf* from financing public goods and mixed public goods?

6. What are the components needed to revive this particular function of *waqf* (i.e. financing public goods and mixed public goods) in Malaysia?

7. If *waqf* is to finance public goods and mixed public goods in Malaysia, can Malaysia be able to reduce its federal government debt?

8. Would you like to give any additional comments?

In the following subsections, reasons for the adoption of semi-structured interviews, sampling of interview, the way interviews are performed, as well as the validity and reliability of interviews are stated.

4.7.1.1 Significance of Semi-Structured Interviews

Semi-structured interview is an appropriate form of data collection due to two reasons. First and foremost, it enables this researcher to probe deeper, thus, enhancing this researcher's understanding on the answers given. Bryman (2012) asserts that semi-structured interviews permit other relevant questions to be asked when the interviewer notices certain things said by the interviewee. Needless to say, the use of *waqf* to finance public expenditure is scarce and the resultant impact on government debt is even more so. Therefore, it is imperative that this researcher uses interview techniques that can enhance the understanding of this research topic. Second, it allows two-way communication between the interviewer and the interviewee which could establish

rapport between the two. Establishing rapport presents the opportunity for this researcher to address sensitive issues and get honest input from the interviewee.

However, one major critic of semi-structured interviews or any form of interviews for that matter is biasness (Leonard, 2003). Bias can originate from both the interviewer and the interviewee. More often than not, the interviewer will have a general expectation on the opinions of interview participants which could affect the quality of research. In turn, the interviewee could have certain preconceptions based on the interviewer's conduct and appearances. This can affect the answers given by the interviewee which in turn will affect the quality of research.

There is no clear-cut way to totally eliminate biasness. For this particular research, bias from the interviewee's side is reduced by choosing interview participants through theoretical sampling. Theoretical sampling or purposive sampling is a valid sampling type and is elaborated in the next section. Meanwhile, bias from the interviewer's side is minimised by establishing rapport so that preconceptions are minimised and the promise of anonymity.

4.7.1.2 Interview Sampling: Theoretical Sampling

Experts of *waqf* consisting of academicians/*Shari'ah* scholars, government officials, and industry experts identified through theoretical sampling or purposive sampling were interviewed. Theoretical sampling requires "the selection of cases on the basis of the researcher's own judgement about which will be the most useful" (Bloor and Wood, 2006, p.155).

In order to come out with the list of interviewees, the references regarding to *waqf* that are cited in Chapter 2 is perused. Starting off with the governing *Shari'ah* of *waqf* in

Section 2.2, amongst the research cited were Kahf (n.d., 2014), Siti Mashitoh (2014), Mohsin (2009, 2013), and Razali (2015). With regards to the application of *waqf* in economics and the public finance sphere of Section 2.3, Çizakça (1998), Mohd Umar et al. (2012), Kuran (2001), Mohsin (2009), Gil (1998), Frenkel (1999), Mandaville (1979), Kahf (2014), Busharah (2012), Pioppi (2004), Shamsiah (n.d.), and Khalil et al. (2014) are amongst the studies referenced. Section 2.4 that pertains to the Malaysian *waqf* practice had cited among others, Çizakça (2000), Siti Mashitoh (2011), Sharifah Zubaidah (2016), JAWHAR (2010a, 2010b), eWakaf Johor (n.d), WSM (n.d.b), PWS (n.d), and WANCORP (2015). Lastly, Section 2.5 that argued the place of public *waqf* in Malaysia mainly cited Mohd Nahar and Mohamed Aslam (2016).

To ensure data saturation, several other interviewees must also be considered. These are in turn identified through recommendations from interviewees and peers as well as online search engine. After omitting those who are unwilling to be interviewed (reasons include retirement, unresponsive interview request, and others), the list of interviewees is tabulated in Table 4.1 below. This number of participants is sufficient as Kvale and Brinkmann (2009) asserts that in common interview research, data were gathered from ten to fifteen interviewees.

Table 4.1: List of Interviewees

Academicians/ Shari'ah Scholars	
Name	**Affiliates**
1. Assoc. Prof. Dr Siti Mashitoh binti Mahamood	Academy of Islamic Studies, University of Malaya
2. Prof. Dr. Monzer Kahf	Qatar Faculty of Islamic Studies, Hamad bin Khalifa University
3. Assoc. Prof. Mustafa Omar Mohammed	Kuliyyah of Economics and Management Sciences, International Islamic University of Malaysia
4. Assoc. Prof. Dr. Magda Ismail Abdel Mohsin	International Centre for Education in Islamic Finance

Academicians/ Shari'ah Scholars	
Name	**Affiliates**
5. Assoc. Prof. Dr. Fuadah Johari	Islamic Science University of Malaysia (USIM)
6. Prof. Mohamed Aslam bin Mohamed Haneef	Kuliyyah of Economics and Management Sciences, International Islamic University Malaysia
7. Prof. Dr. Ismail Ahmad	Faculty of Business Management, Universiti Teknologi MARA Shah Alam
8. Assoc. Prof. Dr. Ahcene Lahsasna	International Centre for Education in Islamic Finance
Government Officials	
Name	**Designation**
9. Mustapahayuddin bin Abdul Khalim	Assistant Director of Waqf, SIRC of Johor
10. Mohd Bokhari bin Mat Doa	Executive, Research and Waqf Product Section, Yayasan Waqf Malaysia (YWM)
11. Damithah binti Iberahim	Senior Officer of Islamic Affairs, Baitulmal Section, SIRC of Federal Territories
12. Haji Zainal bin Haji Mohd Yusof	Awqaf Officer (Development & Finance), Department of Awqaf, Zakat and Hajj (JAWHAR)
Industry Experts	
Name	**Designation**
13. Nasaruddin Ahmad	Executive, Waqaf An-Nur Corporation (WANCORP)
14. Haji Che Mazlan Che Yusoff	Head, *Waqf* Management & Secretariat, Bank Muamalat

Prof. Dr. Monzer Kahf is an expert in *Shari'ah* of *waqf*, past application of *waqf* in economics, and *waqf* financing instruments. Mohamed Aslam bin Mohamed Haneef is a co-author in the article written by Mohd Nahar and Mohamed Aslam (2016). Assoc. Prof. Mustafa Omar Mohammed is an expert on Islamic economics. Assoc. Prof. Dr Siti Mashitoh binti Mahamood is a *Shari'ah* scholar as well as an expert in Malaysian *waqf* laws and practices. Prof. Dr. Ismail Ahmad is an expert in Islamic economics and Islamic finance plus was suggested by Assoc. Prof. Mustafa Omar Mohammed. Assoc. Prof. Dr. Mohsin Ismail Abdel Mohsin has expansive knowledge on *waqf* practices around the globe and *waqf Shari'ah*. Assoc. Prof. Dr. Ahcene Lahsasna is well versed in *waqf*, Islamic finance, and *Shari'ah*. He is also a registered *Shari'ah* Advisor approved by the SC. Meanwhile, Assoc. Prof. Dr. Fuadah Johari is an expert in Islamic social economics.

These combination of *waqf* experts that also have knowledge on different related fields have more vision on *waqf* development. Thus, they provide a coherent and an all rounded view on how *waqf* financing Malaysian public expenditures should be.

It is however not adequate to interview academicians only. Interviewing government institutions of *waqf* will provide clearer understanding on *waqf* practices in Malaysia which will practically help develop the *waqf* idea of this thesis. JAWHAR is under the Prime Minister's Department, hence, the institution has an overall understanding on the *waqf* practice in Malaysia. As the federal government trust body, YWM is more hands on with *waqf* management which will provide extra input for this thesis. The SIRC of Federal Territories, or Majlis Agama Islam Wilayah Persekutuan (MAIWP), is also interviewed to know the manner of *waqf* management in a state that do not promulgate specific *waqf* law. In comparison, the SIRC of Johor were chosen to know the manner of *waqf* management in a state that do promulgate specific *waqf* law. SIRCs are sole trustees of *waqf* that directly manage *waqf* well before the formation of YWM. Thus, interviewing SIRCs are vital because they can share their long experience and knowledge that YWM and JAWHAR might not possess.

Lastly, the industry experts chosen to be interviewed are BMMB and WANCORP. The industry experts are more skilled in Islamic finance and risk management as oppose to government institutions. They also tend to be more practical than academicians. Therefore, industry experts can certainly add depth to the interview results.

4.7.1.3 Interview Administration

The interviews were mostly administered face-to-face either by meeting or conducted through Skype. Another was conducted through email. The interviews were recorded with

permission from the interviewees. Recording allows this researcher to compare answers from different interviewees and perform in-depth analysis later on. Emails and letters requesting an interview were sent beforehand to the interviewees and follow up calls were also made to confirm interview dates. Then one or two days before the interview date, a reminder is sent to the interviewee.

On the day of the interview, questions from the interview guideline that were prepared by this researcher were asked. Whenever the answers given were unclear, this researcher would probe further. Probing questions were also asked when ideas given by the interviewee are new to this researcher. In addition to that, this researcher would provide clarification when the interviewees had difficulty in understanding the interview questions. This can happen in two ways; either the interviewee states that (s)he does not understand the question or when the answer given by the interviewee does not answer the question. In these cases, the interview question is rephrased for clarity.

4.7.1.4 Validity and Reliability of Semi-Structured Interview

Validity is defined as "the extent to which any measuring instrument measures what is intended to measure" (Carmine & Woods, 2004, p.1172). There are three types of validity which are criterion-related validity, content validity, and construct validity (Carmine & Woods, 2004). For this specific research, validity for the qualitative part is ascertained through criterion-related validity and content validity.

Criterion-related validity is attained when findings from a specific measuring instrument follows certain external criterions (Carmine & Woods, 2004). The findings from semi-structured interviews are valid for this study because this researcher makes sure that it has basis from the literature review, findings from the quantitative part, and/or

answers from different interviewees. Meanwhile, content validity describes the degree to which findings from a specific measuring instrument replicates the domain of the topic under study (Carmine & Woods, 2004). For this research, content validity is obtained by acquiring inputs from all *waqf* experts which include academicians/*Shari'ah* scholars, government officials, and industry experts, hence, ensuring that answers obtained replicate the domain of the research as best possible.

On the other hand, reliability means the extent to which consistent result is obtained through a specific measuring method which is almost always associated to quantitative framework only (Payne G. & Payne J., 2004). For the case of this thesis, consistent quantitative result were obtained through inducing different shock values and parameter values as well as confirming the result with the qualitative result. In other words, a small part of this thesis uses methodological triangulation to confirm the quantitative result. On another note, reliability does not concern qualitative framework because "social life is not repetitive or stable, and so our research perceptions of it cannot be entirely consistent" (G. Payne & J. Payne, 2004, p.198).

4.7.2   Quantitative Method: DSGE Model

To reiterate, DSGE model is based on GE equilibrium theory which takes into account the fact that variables do not return to equilibrium instantaneously and permits stochastic process in its model. The DSGE model is run using MATLAB and Dynare. Analysis of DSGE model requires the specification of parameter values and steady state values as well as introduction of shock. Parameter values are obtained either through calibration, extrapolation, and ordinary least squares (OLS) method while steady state values are obtained through simultaneous equation and OLS method. To clarify, calibration simply means obtaining value directly from the literature (Torres, 2013). A brief description of

109

DSGE model analysis is presented in Section 4.8.2 while an in-depth explanation is done in Chapter 7. The followings are the significance of DSGE model, sampling of data for the model, and validity as well as reliability of DSGE model.

4.7.2.1   Significance of DSGE Model

DSGE model is significant to the research process of this thesis due to four major reasons. First, a specific economy can be developed to include *waqf* contributions by household. Second, it allows for stochastic process like that of Equation 4.5. Third and most importantly, an impulse response function (IRF) can be generated that shows the trajectory of debt to GDP ratio in the event that *waqf* finances public expenditures. This directly answers RO 3. Lastly, DSGE model can be assumed as a recently developed technique, hence, this thesis is able to contribute further to the body of literature.

4.7.2.2   Data Sampling

The data used for this study is selected through systematic sample whereby units of data are picked straight from the sampling frame (Bryman, 2012). It must be reminded here that data pertaining to the form of *mawquf* is not yet known. Data on the value of *waqf* usufruct is also not known as the method to guarantee its perpetuity is not known. Therefore, at this point, only data sampling of parameter values and steady state values presented in Section 4.5.1 is discussed.

To be exact, quarterly data from the third quarter of 1997 to the fourth quarter of 2015 were selected for G_t, T_t, and Y_t. G_t is the sum of federal government operating expenditure and federal government development expenditure, T_t is the federal government revenue, and Y_t is the gross domestic product (GDP) prices using year 2000 as the base. These data

are obtained from BNM. Mean household expenditures and mean household income for the year 2014 were obtained from Department of Statistics Malaysia (DOSM) (2015). The value of μ, γ, and ν are extrapolated from there. At the point of writing this thesis, record for the year 2014 is the latest data that DOSM possessed. On the other hand, the value of β, α, and δ are obtained from Torres (2013), Iwata, Khan and Murao (2003), and Nagaraj (2005) respectively.

It is worth noting here that calibration is opted in order to shorten the time span of this study which in itself time-consuming. Furthermore, this researcher is constrained by her sponsorship period. Regardless, calibration is a data sampling technique recognised by Torres (2013) and used by Tourinho et al. (2013).

4.7.2.3 Validity and Reliability of DSGE model

Validity for the quantitative part of this thesis is ascertained through criterion-related validity and construct validity. To reiterate, criterion-related validity is attained when findings from a specific measuring instrument follows certain external criterions (Carmine & Woods, 2004). Findings from DSGE model is valid for this study because this researcher based its theoretical model on the literature review and qualitative findings. Plus results from DSGE model result is then confirmed back with other qualitative findings.

On the other hand, construct validity is "the extent to which a measure performs according to theoretical expectations" (Carmine & Woods, 2004, p. 1173). For this thesis, the theoretical expectation is *waqf* can aid in government debt reduction by employing *waqf* to finance certain federal government expenditures. Hence, for this thesis, the construct validity of DSGE model is that the simulation performed in Chapter 6 shows a

decreased trend in federal government debt which conforms to the theoretical expectations of this thesis.

4.8 Data Analysis Techniques

Data analysis is the process involved in transforming collected data into results. In other words, it is done to answer the ROs, RQs, and tests the hypotheses of this study. Basically, all the ROs are investigated using qualitative analysis but RO 3 is investigated using mainly quantitative analyses. Study of debt sustainability is often done quantitatively and the minor qualitative approach of RO 3 is only opted to confirm the result from DSGE model.

4.8.1 Qualitative Data Analysis Process: Thematic Analysis

In order to attain all the ROs, thematic analysis and interpretive method of analysis are adopted. Although Bryman (2012) asserts that thematic analysis is an emerging method of analysis, Kvale and Brinkmann (2009) as well as Guest, MacQueen, and Namey (2012) claim that this manner of analysis is the most useful in capturing the complexities of meaning from transcribed interview texts. Thematic analysis is a process of making clear the structures and meanings of data by identifying themes from that set of data (Gavin, 2008; Bryman, 2012). Bryman (2012) states that a theme is a category identified by the researcher through data that relates to the RQs of that specific study. Bryman (2012) further adds that the identified category builds upon codes emerging from transcripts which can aid the researcher to make a theoretical contribution to the literature. However, codes and themes can essentially be the same too (Bryman, 2012).

There is no clear-cut way on how one should perform thematic analysis as this approach does not have any distinct strategies or techniques to do it (Bryman, 2012). For this study, the thematic analysis was done as follows. The whole transcript was read first to get a sense of meaning. Then in Microsoft Word, the themes that correspond to this study's research questions were identified and differentiated by using different font colours. By using the "Table" function, condensed answers corresponding to each theme are stated in the second column without losing its meaning while the first column contains the interview transcript. Condensed answers are inputs from interviewees stated in simpler terms. Lastly, in another Microsoft Word document, the different themes and condensed answers are segregated.

The condensed answers are then subjected to interpretive method of analysis. Orlikowski and Baroudi (1991) define interpretive study as the "attempt to understand phenomena through accessing the meanings that participants assign to them" (p.5). Specifically for this thesis, this researcher attempts to understand the meaning of those condensed answers given by the interviewees. The meanings are valid and reliable in accordance to the discussion outlined in Section 4.7.1.4. Biasness was also acknowledged in Section 4.7.1.1.

Thematic analysis using computer softwares such as NVivo and Atlas.ti were not employed due to two reasons. First, it gives the opportunity for this researcher to identify first-hand the relevant themes and omit those that are not. As a result, this thesis will become more engaged with the qualitative data. Second, interpretation of transcribed interviews still needs to be done by the researcher alone because NVivo and Atlas.ti can only identify themes. Hence, using computer software is not entirely necessary.

4.8.2   Quantitative Data Analysis: Eviews, Dynare and MATLAB

RO 3 mainly uses quantitative analysis. In order to test the hypothesis that was stated in Section 4.5.2, the theoretical model of Section 4.5.1 is analysed using two software which are Dynare and MATLAB. A .mod file is written in MATLAB before adding the command line for Dynare. Basically, a .mod file contains four distinct blocks that must be written in order which are preamble, model, steady state or initial values, shocks, and computation (Griffoli, 2007-2008). In the preamble block, variables and parameters used in the model are listed. In the model block, the model equilibrium (explanation regarding model equilibrium is given in Section 7.5) is spelled out. In the next block, the steady states or the starting points for simulation are specified based on the model's solution. Shocks to the model are specified in the shocks block. Lastly, calculation is done in the computation block by instructing Dynare to perform specific operations.

For this study, the specific operation that was instructed to Dynare is simulating the IRF of the Malaysian federal government debt to GDP ratio (B_t) by introducing shock to the model. IRF is the trajectory of every endogenous variables in the model given that these variables move upon shocks. Estimating the IRF for B_t is called for since RQ 4 seeks the answer for the future trend of federal government debt to GDP ratio. Chapter 7 details on the procedures for simulation as well as the result of IRF.

It must be mentioned that another software was also used. Since certain steady state and parameter values were obtained through OLS estimation, the software Eviews was employed.

4.9   Conclusion

Chapter 4 had presented the research process of this thesis thoroughly. This thesis employs mixed methods research because the methodology bests answers the ROs and RQs. As a consequence, results produced are more focused, comprehensive, and coherent. Sequential research strategy with exploratory sequential design is opted because certain data are needed to be obtained qualitatively before they can be examined quantitatively. Although the research period becomes longer, its advantage of answering the ROs comprehensively outweighs the longer research period. The entire thesis is governed based on the conceptual framework designed in Figure 3.10. Meanwhile, the quantitative part of this research is governed by GE theory with a theoretical model based on Neoclassical economics.

Two sets of data are required for this research namely primary data and secondary data. Primary data is collected using semi-structured interviews while secondary data is collected from BNM and various sources of literature. Through thematic analysis, the primary data is analysed in order to answer all the ROs and ascertain variables that are needed for the quantitative analysis. Using Dynare, Eviews, and MATLAB software, the quantitative analysis is performed by analysing the impact of *waqf* financing public expenditure on debt through simulation. Results from quantitative analysis contributes significantly to RO3.

CHAPTER 5: QUALITATIVE ANALYSIS: *WAQF* **FINANCING FEDERAL GOVERNMENT PUBLIC EXPENDITURE**

5.1 Introduction

Most of the past studies focused on the management of Malaysian *waqf*, its laws, and ways to sustainably finance it. However not much has been done on the viability of *waqf* to finance federal government public expenditures. The implementation of *waqf* in such way is quite new and with the Malaysian *waqf* environment that is constantly evolving, other related issues would rise. Thus this chapter would analyse these aspects.

Chapter 5 presents the findings of RO one that corresponds to RQ one and RQ two. To reiterate, RO one is "To explore the extent to which *waqf* financing Malaysian federal government public expenditure is doable". Meanwhile, RQ one is "Why *waqf* financing Malaysian federal government public expenditure is doable?" and RQ two is "What are the issues that could obstruct the use of *waqf* to finance Malaysian federal government public expenditure?" At its basic, Chapter 5 determines the desirability of *waqf* to finance certain components of federal government expenditures in Malaysia. It gauges whether the Malaysian *waqf* practice promotes the creation of public *waqf* and by extension explores the possibility of *waqf* as a means to finance public goods and other social services.

The organisation of this chapter is as follows. Section 5.2 discusses the reasons for viability of *waqf* financing certain federal government expenditures which are *Shari'ah* permissibility, past Islamic economy use of *waqf,* and political will. Section 5.3 highlights the issues that would emerge from the *waqf* implementation in question. The issues are sorted into three themes which are *waqf* laws, *waqf* management, and *waqf* financing strategy. Lastly, in Section 5.4, the conclusion will be made.

5.2   The Viability of *Waqf* Financing Certain Malaysian Federal Government Expenditures

All interviewees agreed to the idea of *waqf* financing certain public expenditures except one interviewee. Academician A during a personal interview on 24th January 2016 said that:

Now why should a person in Malaysia make *waqf* to help the government budget? Because, it is possible that some time the government may use it in a wrong way, for extravagant expenses. I'd rather, anybody I think, would be rational to make *waqf* for education, to make *waqf* for hospital, to make *waqf* for improving the roles in the country, or in any area of the country, that is specifically for something that is good.

The interviewer disagrees because of potential mismanagement by the government. To put it specifically, Academician A acknowledged that *waqf* can finance public expenditure but due to potential government mismanagement, disproves of the idea. The acknowledgement is elucidated by Academician A upon reflecting on the governance of Umar ibn Khattab:

We have an example that there was in fact where *waqf* had clearly helped public finance that was considered the revenue of the budget. That was what Umar ibn Khattab did in creating the *waqf* of the lands of the newly conquered lands. And he said this is the *waqf* for the *ummah* or to support its budget. From it yes, budget has continuously and classically financed by this *waqf*.

Gil (1998) attested to this statement.

Anyhow, the stand of Academician A pertaining to government corruption is founded in the literature. The issue of government corruption has indeed been recorded in history and had become one of the deterrents for *waqf* development (Peri, 1992; Baer, 1997;

Babacan, 2011; Çizakça, n.d.). Still, it was also argued in Section 2.3.1 that corruption is an isolated problem that can manifest in both public and private sector institutions. The argument was based on the claim of Baer (1997) that *nazir khas* were trying to control public goods and received large portion of income from *waqf*. Thus, this thesis recognises the issue of mismanagement but would be prejudice to associate mismanagement with the federal government per se. Instead, it would be fair if proactive steps are instituted to combat corruption in all forms of organisation. For instance, the Malaysian Anti-Corruption Commission could carry out corruption prevention measures on the government level while accounting audit can be carried out on the private level. Regardless, this is only a general recommendation. This issue of mismanagement is succinctly addressed in Section 5.3.2 and Section 6.2.2.

On the other hand, the arguments in support for *waqf* financing public expenditures can be based on three major themes. These are *Shari'ah* permissibility, past Islamic economy use of *waqf,* and political will.

5.2.1 *Shari'ah* **Permissibility**

All interviewees that agree to the implementation of *waqf* in question unanimously agree that there is no *Shari'ah* contradiction to employ *waqf* to finance public expenditures. In the words of Academician C during a personal interview on 5th April 2016, "I cannot see any *Shari'ah* issue as long as you observe all the *Shari'ah* requirements and the laws that would be fine". This is a solid support of the idea for *waqf* financing certain federal government expenditure in Malaysia.

The *Shari'ah* requirements are the principles and the pillars of *waqf* which was outlined in Section 2.2.1 and Section 2.2.2. To reiterate, the principles are irrevocability,

perpetuity, and inalienability while the pillars are *waqif, mawquf, mawquf 'alaih, sighah,* and *mutawalli.* The modus operandi for *waqf* financing public expenditure is legitimate so long as these aspects were accounted for. Besides that, the claim by Ebu's Su'ud that *waqf* follows the contemporary custom (Imber, 1997) provide further justification for the implementation of *waqf* in question. Since it is the contemporary norm for the federal government to provide public goods, mixed public goods, and other social services which can expectedly become the purpose for *waqf*, then by extension, *waqf* financing public expenditures is permissible.

However, Academician H during a personal interview on 10th August 2016 believed that caution must be exercised:

It is the government's function to take care of the public. So if we put *waqf* in the position where we move the government's burden to society, I do not agree. But if *waqf* assume a complementary role then it can be [instituted]… It is not that *waqf* must take care of society and government should divert its function.

To put it concisely, *waqf* should only play a complementary role and it should not be mandatory for *waqf* to care for public goods and related others. It is important to remember that *waqf* is a third sector instrument thus is dissimilar from tax. As such, the strategy of *majhud dhati* or *juhud dhatiyya* employed by Egypt is not suitable for Malaysia.

In terms of laws, Academician C was referring to the Malaysian *waqf* laws. Specifically, the implementation of *waqf* for financing certain federal government expenditure must not disregard the difference in *waqf* laws of each state. A mechanism to accommodate these laws thus should be thought of. Note that there already exists *waqf* enactments that are progressive in nature such as clauses that allow the appointment of

nazir khas, financial instruments as the capital for *waqf*, and others. It begs the question whether specific *waqf* enactments should be promulgated for each state? Should *waqf* laws for financing public expenditure be streamlined? If so, how can that be achieved? These complications in *waqf* laws are comprehensively address in Section 5.2.1 and Section 6.2.1.

5.2.2 Past Implementation in Islamic History

The second justification for the idea of *waqf* financing certain federal government expenditures is its successful implementation in past Muslim economies. This was recognised by Academician A during a personal interview on 24th January 2016, Academician B during a personal interview on 7th January 2016, Academician G during a personal interview on 31st March 2016, Government Official A during a personal interview on 7th June 2016, Government Official B during a personal interview on 10th March 2016, and Industry Expert B during a personal interview on 18th January 2017. In the words of Academician G:

> You see when we talk about *waqf* and go back to the Ottoman experience, they use *waqf* and they also use cash *waqf* even to finance the economic, precisely to finance the army and military force. It has been used, yes and it was successfully done, yes and it can happen again because the concept is the same.

As was reviewed in Section 2.3.1, pure and mixed public goods as well as other related goods were successfully supplied through *waqf* which included defence, water supply, education, training, healthcare, animal care, and transportation among others (Peri,1992; Çizakça,1998; Gil, 1998; Kahf, 2014). During the time of the Ayyubid Dynasty, *waqf* was formally introduced as a public policy that lasted through the Ottoman era (Frenkel,

1999). These had led Faridi (1983) to believe that *waqf* has its role as a third sector constituent in an ideal Islamic economy. Thus as a Muslim majority country, it is only given that Malaysia can apply this idea of *waqf*. As a matter of fact, Section 3.2 has identified the components of federal government expenditures that are suitable for *waqf*. The components are subsidies and all items in federal government development expenditure except for general administration.

Furthermore, the third sector concept in modern economics is not a notion that is unique to Islam. There is an explosion of studies with regards to the third sector in Europe. A compilation of this studies can be found in Evers and Laville (2004). As was alluded in Section 2.5, Pestoff (1992) had shown how the state had employed the assistance of TSOs to carry out certain state duties. Besides, Shaham (1991) claimed that non-Muslims had also practiced some form of *waqf* during the late Ottoman era. Thus for a country consisting of various religion, to employ the assistance of *waqf* to finance for public expenditures is practically applicable.

5.2.3   Political Will of the Federal Government

The third and most solid support for the implementation of *waqf* in question is the evidence of a political will. Government Official A during a personal interview on 7th June 2016 and Government Official B during a personal interview on 10th March 2016 confirmed this. Government Official A and Government Official B respectively claimed that:

Even now, the [federal] government is looking forward to corporate *waqf*. Of recent, the Prime Minister himself did mention that corporate *waqf* should be develop further. Meaning eventually, it [*waqf*] will assist the federal government. It's just in Malaysia,

waqf is under the jurisdiction of the state. So development [of *waqf*] only involve

states. As for the federal government, *waqf* collection is still at the initial stage.

Our grand view is, *waqf* will in the future replace a lot of sectors such as health,

education. This leaves the federal government to focus on others that are more

important… Therefore [*waqf*] can lessen the government's burden.

This is also the belief of Sanep and Nur Diyana (2011) when the federal government

had taken the initiative to endow *waqf irsod* following the Ninth and Tenth Malaysia Plan.

Through *waqf irsod*, shop lots, low cost housing units, education complex, and orphanage

were successfully built on *waqf* land by JAWHAR which make up public goods and social

services. The undeniable fact is, although SIRCs are the sole trustees of *waqf*, adaptations

were found so that federal government bodies (JAWHAR and YWM) can jointly develop

waqf with SIRCs. In the case of Larkin Sentral Property Berhad for instance, the SIRC of

Johor remains as the general manager of *waqf* or *nazir am*. Therefore, ways can certainly

be found so that *waqf* financing certain federal government expenditures can harmonise

with the Malaysian *waqf* laws. The initial phase of this implementation is already taking

place.

Another indication of political will sourced from the literature is the publication of six

waqf manuals by JAWHAR in order to promote best practices in Malaysian *waqf*

management (Sharifah Zubaidah, 2016). As stated in Section 2.4.2, there are six of these

manuals. This effort had prompted a few SIRCs to revise their laws on *waqf* to be more

progressive. To reiterate, these laws are *Wakaf* (State of Selangor) Enactment 2015 and

Wakaf (State of Perak) Enactment 2015. Johor, Malacca, and Negeri Sembilan are more

proactive in the sense that their *waqf* law has already been revised even before these

manuals were published. Most of these laws had resulted in the creation of more public

waqf that was discussed in Section 2.4.4. In relation to this, there was an attempt to instate

Federal Territories *Waqf* Act to make Malaysian *waqf* laws uniformed through Article 75

of the Federal Constitution, but it was unfruitful even after 12 years of negotiation (Sharifah Zubaidah, 2016). An in depth discussion of *waqf* laws are provided in Section 5.3.1 and Section 6.2.1.

On top of that, the Malaysian federal government had decided to reduce its expenditure in an effort to combat growing debt. A direct result from this is the enumeration of the National Higher Education Strategic Plan 2020 that urged public universities to acquire various sources of funding. As was explained in Section 2.4.4, *waqf* had become one such source. Zurina, Zamir and Mustafa (2016) had listed nine institutions of higher learning that employ the use of *waqf* fund. In fact, a *waqf* fund for University of Malaya has already been established upon the date of this writing. Academician C during a personal interview on 5th April 2016 had alluded to the establishment while providing evidence of government will to employ *waqf*:

> This is because the government now is giving its support. The government is inclined to introduce *waqf*. Even in University of Malaya (UM), application for consent has already been sent at the SIRC of Federal Territories and approved. UM will establish a *waqf* fund.

As such, there is a high possibility for the establishment of *waqf* fund in other fields too in the near future. Ainul Kauthar, Arieff and Azman (2014) for instance, had analysed on the potential of *waqf* for the Malaysian health sector. Duly note that health is a component of federal government expenditure.

5.3 Issues Concerning *Waqf* Financing Public Expenditures

Although the idea of this *waqf* implementation is doable, it is not without issues. The issues are described based on three themes. These themes are *waqf* laws, *waqf*

management, and *waqf* financing strategy. These issues can have a different impact on *waqf* for public expenditure and are deliberated in subsequent sections.

5.3.1 Malaysian *Waqf* Laws

Almost all interviewees commented that the Malaysian *waqf* laws will be an issue except for Academician H. However, comments from the interviewees regarding this are multifaceted.

All state statutes declare that SIRC is the sole trustee of *waqf* in Malaysia. In other words, the SIRCs are tasked with the supervision, management, and development of all *awqaf* assets in Malaysia. Thus by extension, SIRC is also the trustee for *waqf* financing public expenditure. To do so otherwise is illegal. Still, Academician A, Academician F (interviewed on 20th March 2016), Industry Expert B, and Academician G are not in favour of this. Academician A and Academician G respectively asserted that:

So the *Deen* council (SIRC) are great impediment of *awqaf* in Malaysia and the management of *awqaf* should be freed, determined only by the founder of the *waqf*… add *waqf* independent of decree from the government. Like any other NGOs.

We have some legal constraint from *waqf* as you know, any *waqf* that is declared will be under the authority of *Majlis Agama*, the State Islamic Religious Councils which has a back institution that is the sole custodian to take over this one.

Academician F had also reprimanded strongly the role of SIRC as the sole trustee of *waqf*:

Even they can't manage their own administration, what more they want to manage many other things? Right? So, there has to be a serious reform in MAIN (SIRC) setup in order for *waqf* to play a bigger role.

Of course, states that permit the appointment of *nazir khas* and/or joint collaboration with private sectors are excluded which are Selangor, Negeri Sembilan, Malacca, and Johor. Selangor, Negeri Sembilan, and Johor in particular, saw a rise in public *waqf,* a category where *waqf* for public expenditure belongs. This is mainly because *nazir khas* have more experience and knowledge in financing modes. JCORP in Johor had even penetrated the Islamic Capital Market via IPO of *waqf* of shares. Academician C during a personal interview on 5th April 2016 pointed out this fact:

> Although *Majlis* (SIRC) is the only trustee, sole trustee and only *Majlis* can manage *waqf* property but in the law, there are clauses that state the *Majlis* can give written permission to do this given certain conditions. A lot of clauses that support this fact that not many know.

Among the clauses that Academician C meant are the provision from *Wakaf* (State of Negeri Sembilan) Enactment 2005 and *Wakaf* (State of Selangor) Enactment 2015. The effects of these clauses on the creation of public *waqf* have been argued extensively in Section 2.4. Section 33(1)(a), 33(1)(b), and 33(1)(c) from *Wakaf* (State of Negeri Sembilan) Enactment 2005 states that:

(1) The Majlis, on the advice of the Advisory Panel, may—

> (a) appoint any person whom the Majlis reasonably considers competent and qualified to manage and develop any mawquf, including to manage investments of the mawquf;
>
> (b) appoint any person whom the Majlis reasonably considers competent and

qualified to manage the benefit, interest or profit of any mawquf in the interest of its mawquf-alaih; and

(c) appoint any agent whom the Majlis reasonably considers competent and qualified, whether a solicitor, banker, licenced financial advisor or any other person, to execute any transaction required in managing the affairs of wakaf.

Meanwhile, Section 4(1)(a), section 4(1)(b), and section 4(1)(c) of *Wakaf* (State of Selangor) Enactment 2015 stipulates that:

4. (1) The Majlis shall be the sole trustee for all *wakaf* situated in the State of Selangor and shall have the powers to—

(a) establish a Corporation;

(b) appoint or give written permission to any person to become the administrator or manager and hold any mawquf on his behalf; and

(c) declare the appointment of any administrator or manager in situation where waqif has appointed his own administrator or manager subject to the terms and conditions prescribed by the Majlis

Aside from these stipulations regarding *nazir khas*, *waqf* enactments and *waqf* rules also contain other progressive clauses. For instance, Section 17 of *Wakaf* (State of Malacca) Enactment 2005 states that, "The Majlis may offer wakaf shares of any property obtained or to be obtained by it to any person for such shares to be purchased which is subsequently endowed as a wakaf to the Majlis". Johor, a state that is the pioneer of *waqf* shares, had long acknowledged its permissibility through Section 2 of Johor Wakaf Rules that was established in 1983. On top of that, Section 23 of the *Wakaf* (State of Selangor) Enactment 2015, Section 2 of the *Wakaf* (State of Malacca) 2005, and Section 13 of Johor

Wakaf Rules allow persons to endow company shares termed as *waqf* of shares. In fact, Section 23 of the *Wakaf* (State of Selangor) Enactment 2015 also includes other financial securities like *sukuk*:

(1) The Corporation may accept—

(a) shares, bonds, sukuk or other instruments for valuable guarantee; and

(b) benefits from the units of share, bonds, sukuk or other instruments for the said valuable guarantee,

given by way of *wakaf* by any person, society or institution provided that the business or investment carried out is consistent with Hukum Syarak.

(2) Any property acquired or developed from the proceeds of sale of shares, bonds, sukuk or other instruments for valuable

guarantee under paragraph (1)(a) shall be a *mawquf*.

This specification of financial instruments show that *waqf* laws are up to date with contemporary economics and financial setting.

Therefore, the disapproval of Academician A, Academician F, Academician G, and Industry Expert B towards SIRC as the sole trustee are related to the states that have stagnant *waqf* laws or do not promulgate *waqf* enactments nor *waqf* rules. These states are the Federal Territories, Sabah, Sarawak, Kelantan, Kedah, Terengganu, Pahang, Penang, and Perlis.

No stipulations were found in Administration of Islamic Law (Kedah Darul Aman) Enactment 2008 that allow other parties to manage *waqf* nor other clauses that indicate progress. Similarly, none was found in Council of the Religion of Islam and Malay

Custom (Kelantan) Enactment 1994, Administration of the Religion of Islam (Perlis) Enactment 2006, Administration of Islamic Law Enactment 1992 (State of Sabah), Majlis Islam Sarawak Ordinance 2001, Administration of Islamic Religious Affairs (Terengganu) Enactment 2001, Administration of Islamic Law (Federal Territories) Act 1993, Administration of Islamic Law (Pahang) Enactment 1991, and Administration of the Religion of Islam (State of Penang) Enactment 2004. These are evidences of limited *waqf* clauses.

Then again, some states such as Pahang and Penang that have no specific *waqf* enactments nor *waqf* rules are still capable of developing public *waqf*. SIRC of Pahang listed education and agriculture as one of its *waqf* projects (eWakaf Pahang, n.d.) while SIRC of Penang lists housing and commercial buildings as one of its completed projects (Dana Wakaf Pulau Pinang, n.d.). However, the projects by SIRC of Penang were only capable to be developed through budget allocation from the federal government and not independently. It demonstrates the fact that collaboration with private sector can actually assist SIRCs with financial matters. The same goes to SIRC of Pahang where a joint collaboration can possibly increase the return from *waqf* and projects that are public *waqf* in nature.

Despite limited *waqf* clauses in most states, Government Official B defended the role of SIRC as the sole trustee of *waqf*. In the opinion of Government Official B, the law is there for the protection of Malaysian *waqf*:

Meaning s(he) endows *waqf* for the family's use. We won't stop it. It's just, to avoid corruption, misuse, or family feud, it is better that the said *waqf* be registered with the SIRC. When it is registered, should there be any claim in court, the court will favour SIRC because that *waqf* has been registered. So in state statutes, it has been detailed that SIRC is the beneficial owner of state *waqf* lands.

For instance, the case of "Permohonan Pengisytiharan" (2008) pertaining to the Land Concession of Chenderong was in favour of SIRC of Terengganu since the land was vowed as *waqf* in 1941 in accordance to Islamic Wakaf Validity Enactment 1972 and Enactment No.10/1972 of Terengganu. On the other hand, another case involving verification claim of a cemetery land in Shah Alam was dismissed because the first respondent had never intended to vow the land as *waqf* in accordance to Wakaf (State of Selangor) Enactment 1999 ("Permohonan Interlokutari", 2012). Since the land was not registered with SIRC, the status of *waqf* had never been recognised and thus could not be protected.

Regarding court disputes, Academician B brought up an intuitive issue that will implicate *waqf* for public expenditures, "And the third thing is in case of disputes, how will it be settled. Is it the civil or is there any *Shari'ah* Board, is what?" To understand this issue, take notice of Item 1 of the Ninth Schedule under List Two-State List of the Federal Constitution. It does not cover matters such as defence, economics, finance, and other components that relate to the federal government expenditure although they involve Muslims' testate and intestate distribution of assets. Siti Mashitoh (2011) had also pointed this out. Furthermore, Item 1 also state that *Shari'ah* courts has jurisdiction only on Muslims. Thus, the dilemma raised by Academician B can also be stated like this; *waqf* disputes is settled in *Shari'ah* courts but public expenditure does not, so in which court do disputes pertaining to *waqf* financing public expenditure will belong? Similar issue also arises when *waqf* disputes involve non Muslim plaintiff because the *Shari'ah* courts, according to Item 1 of the Ninth Schedule under List Two-State List of the Federal Constitution, only applies to Muslim.

Rohayu and Razali (2009) as well as Razali (2015) had discovered the root cause of this complication. Due to the separation of *waqf* and economics instigated by Western

imperialism, *waqf* becomes known only as an instrument suitable for pure religious purposes. As such, the promulgation of law becomes detached like contained in the Ninth Schedule under List Two-State List of the Federal Constitution. In this case, measure such as a standardised law of *waqf* like that of IBA 1983 should be well thought out. Markom et al. (2013) alluded that IBA (1983) managed to be instituted because banking is enumerated in Items 7 and 8 of the Federal List in the Federal Constitution. Hence *waqf* for public expenditure may as well be instituted according to other Items in the Federal List. Anyhow, a serious deliberation regarding this issue is done in Section 6.2.1.

Focusing back on the issue of SIRC as the sole trustee of *waqf*, Industry Expert A during a personal interview on 16th November 2016 also condones this law. When asked whether SIRC is capable to manage *waqf* for public expenditure, Industry Expert A had answered, "In my opinion, if it concerns state X, I would say yes because there is endorsement from our leadership". State X is a state that has progressive *waqf* laws. In other words, SIRC as the sole trustees of *waqf* will only be an impediment when it refuses to enact clauses that are consistent with current economic and financial circumstances.

Still, there is a possibility that *waqf* financing public expenditures could alter the fundamental structure of the Malaysian *waqf* laws. As envisioned by Academician B:

The biggest issue I told you is the fundamental structure between the state government and the federal government. How are you going to work out those, manage those projects? Will it be the state or the government? So if it's going to be the government then how do we work that out?

Although Academician C stressed that the differences in *waqf* laws should be respected and accustomed, but to what extend can it be practically done? Note that *waqf* financing public expenditures concerns the whole of Malaysia and thus all states.

Ultimately, an assessment regarding the current differences in *waqf* law is warranted to find out whether bureaucracy, transparency, and fulfilment of the founders' will is diminished or heightened within the current legal framework. Government Official A for one, believes that the current legal framework is suitable for *waqf* financing public expenditure but admits that it needs further involvement from the federal government:

The current legal framework in Malaysia can be employed. But the federal government must have more vision [in it], the federal government must acquire more role in the legislation for that purpose [i.e *waqf* financing public expenditure].

On top of that, Industry Expert B had brought out another related issue that is important to be considered, "None or less progressive fatwas for the sake of *waqf* development could deter private sector involvement in public finance." This is especially related to the states that do not stipulate specific *waqf* laws thus requiring constant fatwas from the state's mufti office. For instance, Section 54 of the Majlis Sarawak Ordinance 2001 stipulates that:

If, in the opinion of the Majlis, the meaning or effect of any instrument or declaration creating or affecting any *wakaf* or *nazir am* is obscure or uncertain, the Majlis may refer such instrument or declaration to the Lembaga Fatwa for its opinion as to the meaning or effect thereof, and it shall act on any opinion so given by the Lembaga Fatwa.

This is unlike Section 19 to 26 of the *Wakaf* (State of Selangor) Enactment 2015 that detailed on the kinds of instrument suitable for *waqf*.

Upon analysing the interview transcript further, Industry Expert B was also alluding to issues regarding *waqf* implementation such as *istibdal*, assets suitable for *mawquf*, and others. It is to the believe of Academician H that issues such as these has already been

settled, or at least not a significant issue, "*istibdal* has been debated a lot by academicians and the way out is already clear so it is not a major issue, actually". In fact, when asked whether there are any other issues, Academician H could not come up with one.

Industry Expert B was also referring to the issue of *waqf* investment as is natural for a financial institution. Since *waqf* for public expenditure is an idea of fiscal magnitude, sustainable income is essential and investment is one such method to generate income. Although the OIC Fiqh Academy in its Resolution No.140 (15/6) permits *mawquf* investment in both low and high risk instruments, JAWHAR (2015) had not recorded similar fatwas for Malaysia. In the case of cash *waqf* for instance, JAWHAR (2010a) only endorsed that cash *waqf* be exchange to immovable properties. When enquired whether collected cash *waqf* were invested, Government Official B during a personal interview on 10th March 2016 answered:

> Since the *waqf* in question is not high in value, we only put it in a fixed deposit account, short term, meaning we can take it out whenever we like. [We employ] short term and low risk because the main purpose of *waqf* is not to invest but to obtain *waqf* and exchange it.

However, cash *waqf* investment are being employed by at least one private institution in Malaysia. As divulged in Section 2.4.3, a portion of WSM's cash *waqf* fund is allocated for investment. Perhaps the management committee of WSM made Resolution No.140 (15/6) of the OIC Fiqh Academy as the basis and argument for it.

Another issue that relates to *waqf* law is the law pertaining to *waqf* lands. Malaysia possesses an abundance of *waqf* land (Mohamad Zaim et al., 2015) thus emerging issues should be minimised or eliminated to realise the lands' full potential. In the case of this thesis, the potential to be used as *waqf* for public expenditure could be compromised.

Government Official B admitted that the law on *waqf* land is a timeless issue, "The typical hindrance that will be faced is the issue relating to Malaysian *waqf* lands. There are a number of issues relating to this". Academician C during a personal interview on 5th April 2016 named a few:

> For example, any landed property is attach to National Land Code. National Land Code requires the payment of land tax and others. So these things the federal government should consider giving exemptions of tax, quit rent, and others. Land tax, assessment fee, and other taxes. Plus there are many acts [related to land].

Sharifah Zubaidah and Nor Asiah (2014) had argued the same. Although *waqf* lands are acknowledged in Section 4(2)(e) of the National Land Code (NLC) (Act 56 of 1965) of Malaysia, "Except in so far as it is expressly provided to the contrary, nothing in this Act shall affect the provisions of - (e) any law for the time being in force relating to wakaf or bait-ul-mal", this law is not applicable to the administration of *waqf* lands. In addition, Section 64 (1)(2) stipulates that:

> (1) The reservation of any land for a public purpose (whether effected under this Act or the provisions of any law in force at any time before the commencement thereof) may, subject to sub-section (2), be revoked by the State Authority at any time, either as respects the whole of the land or as respects any part or parts thereof.

which means leased *waqf* lands are vulnerable to appropriation. Example of a leased *waqf* land can be found in Shah Alam whereby a housing project has been initiated (Kerajaan Negeri Selangor, 2015).

Still JAWHAR (2010b) state that the *waqf* lands can be safeguarded through statutory vesting as contained in Section 416C(1) of the NLC:

(1) Where the whole or a part of any alienated land held by the transferor is occupied, used, controlled or managed by the transferee under any right or entitlement derived by way of a donation, gift, bequest, permission, consent, or otherwise howsoever, from the transferor or any predecessor in title of the transferor for any of the statutory purposes of the transferee immediately before the statutory vesting takes effect, the transferee's right to such occupation, use, control or management shall, upon application in writing by him to the Registrar, be endorsed on the register document of title to the land, where the Registrar is satisfied that the statutory vesting of such right or entitlement in the transferee has taken effect.

In the case of *waqf,* the transferee is the SIRC. However, if *waqf* lands were not registered with the SIRC, Section 416C(2) holds that Section 416C(1) will not be binding:

(2) The right endorsed on the register document of title under subsection (1) shall have effect from the date on which the statutory vesting took effect and shall subsist throughout the duration of that title and be binding on every subsequent proprietor of the land.

There indeed exist *waqf* lands that had only been stated verbally to the head of village (Sharifah Zubaidah & Nor Asiah, 2014). In this situation, the *waqf* lands are not secure.

On top of that, JAWHAR (2010b) pointed out that Section 5 of the NLC does not recognise *waqf* as a trust, ""trust" does not include a *wakaf* created in accordance with the principles of Muslim law". Hence, the phrases "*waqf*" and "SIRC as the sole trustee" cannot be transcribed in the document of land title when registering for statutory vesting. In other words, the lands will not be formally known as *awqaf* on paper.

As such, Malaysia actually lacks comprehensive laws that can govern and protect *waqf* lands efficiently. Should the idea of *waqf* for public expenditure materialised in which *waqf* lands were to take part, these issues could convolute the perpetual nature of *waqf*.

5.3.2 *Waqf* Management in Malaysia

Interviewees are also concerned with the existing governance of *waqf* in Malaysia, whether it is suitable for *waqf* financing public expenditure or not. Various concerns were expressed by Academician A, Academician E, Academician F Academician G, Government Official C, Industry Expert A, and Industry Expert B. These concerns can be themed into human resource problems, bureaucracy, and lack of transparency.

The problem of human resource stems from two aspects which are insufficient know how and broad job scope. As stated by Academician E during a personal interview on 29th February 2016:

I'm not going to undermine those in the religious authority department but majority are in the background of *shari'ah* or the background of *usuluddin* probably but they are little in the area of *muamalat*, the practical area... to make the *waqf* to be productive.

The term *muamalat* encompasses the knowledge in Islamic finance, economics, and project execution. Academician B argued along the same lines, "you are talking about an organisation (SIRC) that requires a kind of new outlook, new thinking, so the human capital that should manage this should improve". Academician F gave some specifics, "you need people, you need qualified manpower who basically understand about *waqf* and know how to run *waqf* and manage *waqf* and report and so on". These claims that SIRCs do not possess sufficient human resources with required expertise is also founded in Sohaimi and Syarqawi (2008) as well as Rohayu and Rosli (2014).

It is beyond doubt that *waqf* for public expenditure requires detail planning and execution. This is because the idea involves different public expenditure which are under supervision of a host of ministry departments not to mention the different state *waqf* laws. Hence a workable management procedures that can ensure public goods provision to the beneficiaries is essential. Industry Expert A summed this up into one question, "Issue of appointment, who are we going to appoint as the supplier (of public goods etc.) and the way they are distributed?" To answer this question, at the very least, human capital with knowledge on project management and strategic management is required.

On top of that, this application of *waqf* is more economic in nature and beneficiaries are nationwide. Hence financial and economic strategy are also vital as alluded by Academician C:

> The *waqf* manager should explore using Islamic financial commercial transaction principle to develop *waqf* property not just you know relying on the classical application… There many applicable methods such as *sukuk,* Islamic bond, *waqf* REITs and also contracts such as *waqf* shares, *waqf* of shares, corporate *waqf,* movable *waqf,* immovable, cash *waqf*, and others.

These various financing modes and more, is only comprehensively known by Islamic financiers and Islamic financial engineers. Without these expertise, the management has restricted choices for *waqf* development and income for *waqf*. It is after all vital that *waqf* can generate return to remain sustainable and continually benefit Malaysians.

Secondly, the few employees of SIRCs already have a broad job scope to carry out. Academician G is of the opinion that:

I think the easy way [to apply *waqf* for public expenditure] is to bring the state councils as a member in basically all the operations in the endowments project or whatever projects which is too much, I guess.

It will be "too much" because SIRC also needs to supervise matters of *zakat*, *baitulmal*, marriage, divorce, inheritance, and other Islamic religious duties that is outlined in Item 1 of the Ninth Schedule under List Two-State List of the Federal Constitution (Sohaimi and Syarqawi, 2008).

Government Official C had admitted to this:

Then in terms of employees that should develop these *waqf* properties are also lacking, especially the *Baitulmal* division which is only six people... Now the initiative of SIRC of X regarding the Development and Investment Division is the establishment of a *waqf* centre. The general objective of this centre is to develop [immovable] *waqf* property in state X. However, the centre has only one staff so it is difficult for the staff to carry out the matters of *waqf*.

Further according to Government Official C:

As for the process of receiving fund [from the public], whether it be *waqf am* or *waqf khas*, the application is usually through *Baitulmal*. So when we get the fund or real estate or any form of *mawquf*, we will handle it until it is settled. The money will be given to the Finance Division or if the *mawquf* is immovable property, we hand it to the Development and Investment Division… Meaning we are multipurpose. We have a broad job scope including the projects, their upkeep, their rent meaning we do not focus merely on *waqf*.

As is quoted above, the *Baitulmal* division that consist of only six people have to handle movable *waqf* applications from start to finish and from all fronts. Not to mention that there is only one staff at the *waqf* centre.

In terms of *waqf* for public expenditure, this broad job scope issue can lengthen the process of *waqf* and causes inefficiency if not solved. To explain further, few staffs that already have broad job scopes certainly cannot cope with the *waqf* management involving *waqf* endowments from individuals all around Malaysia. This include figuring out a financial strategy that can guarantee perpetuity and distributing the *waqf*'s usufruct to beneficiaries nationwide. Even if it can be done, the process will be longer and becomes inefficient. Inefficiency may deter future public contribution of *waqf*. These are all unwarranted situations.

To be fair, some SIRCs already attempted to tackle this issue of human resource. For instance, SIRC of Selangor had collaborated with Nada Sepakat Corporation (M) Sdn. Bhd. to build housing units on a *waqf* land in Shah Alam (Kerajaan Negeri Selangor, 2015). Meanwhile, SIRC of the Federal Territories, Malaysia Pilgrimage Fund Board (Lembaga Tabung Haji), and Bank Islam Malaysia Berhad had collaborated together to develop Imarah Wakaf in Kuala Lumpur through the concept of Built Operate and Transfer (BOT) (Edbiz Consulting Limited, 2015). Perhaps the mobilisation of *waqf* for public expenditure requires collaborations from different parties too.

Anyhow, broad job scope can lead to lengthened bureaucracy as the application process of *waqf* becomes longer. Lack of human resources that have experience and knowledge in strategic management further cause inefficiency. These can cause negative public perception and deter the public from endowing *waqf*. Academician E indicated this issue of bureaucracy, "Yes, we always fall down with bureaucracy" and Academician G:

In the past, anyone can just declare *waqf* his house, the hotel, the other one lands, well, anything easy to create. But now the protocol, the legal constraint if you declare as *waqf* today and by tomorrow it's taken by the parties so everyone is reluctant to do that.

What is meant by "taken by the parties" is SIRC as the sole trustee who indirectly acts as the custodian of any *waqf* in Malaysia even though the founders have the intention to appoint other trustees. Although certain enactments such as Section 4(1)(a), 4(1)(b), and 4(1)(c) of *Wakaf* (State of Selangor) Enactment 2015 dictates that a *nazir khas* can be appointed, the founder still has to apply and go through a set of procedures. This very issue could lead to a situation where a founder has the intention to endow *waqf* for public expenditure but also wish to employ a different trustee.

However, the most typical example of bureaucracy is the procedures for converting land title. This was mentioned briefly by Academician C, "For example, any landed property is attach to National Land Code. National Land Code requires the payment of land tax and others... Plus there are many acts [related to land]". Anan (2012), Sharifah Zubaidah and Nor Asiah (2014), as well as Rohayu and Rosli (2014) attest to this fact. The legislation process of converting the land into *waqf* is time consuming and confusing as it can be performed through different methods. In turn, the different methods has a different set of procedures. These different methods are transfer ownership of land, surrender of land, statutory vesting under Section 415(1)(a) of the NLC, and statutory vesting under Section 416C of the NLC with its set of procedures elaborated in the following (JAWHAR, 2011).

Transfer of ownership requires the *waqif* to fill up Form 14A, NLC and submit it to SIRC with other related documents. A process fee must also be paid to the respective Land and Mines Office. Meanwhile, the surrender of land requires the *waqif* to apply for

surrender using Form 12A should it pertain to all parts of land or Form 12B should it pertains to some parts of the land. After approval is obtained from the State Authorities, only then can SIRC apply for the mentioned land as wished by the founder. The State Authorities can then grant the land to the SIRC or convert the land into a reserve and appoint SIRC as the controlling officer (*pegawai pengawal*). If there are any tenancy exempt from registration on that *waqf* land, the original owner of that land must obtain written permission from all involved parties before registration of surrender can be culminated. The surrender process is also subjected to processing fees. On the other hand, statutory vesting under Section 415(1)(a) of the NLC requires the SIRC to fill up Form30A, NLC and submit this form together with other related documents to the Registrar. The Registrar will then proceed to register a statutory vesting in the name of SIRC. This method is also subjected to processing fees. Lastly, statutory vesting under Section 416C of the NLC requires the founder to fill up the *waqf* deed form and submit it together with other related land documents to SIRC. SIRC will then proceed to apply statutory vesting at the Registrar. Unlike the others, the State Authorities can waive any processing fees under this method.

It is obvious that statutory vesting under Section 416C of the NLC is the simplest method to convert a land into *waqf*. However, it is not incumbent on the states to follow this method. Relating back to the case of *waqf* for public expenditure that involves nationwide execution, the difference in procedures from different states could certainly create disarray.

In addition, lack of transparency could pose as another deterrence for *waqf* financing public expenditure. This issue was stressed by Academician A, Academician E, Academician F, and Academician G. Academician A believed that a specific law transparency must be tackled to ensure the integrity of *waqf*:

We need a law of *waqf* to regulate its establishment, to regulate its management, to control, or to subject rather its management to very strong auditing, that maintain the integrity of the property and its use or its objective that avoids corruption that is needed.

Academician E envisioned that transparency can provide a clear modus operandi for *waqf* financing public expenditure in the future:

… the government should have very clear governance of this *waqf* in terms of for example, the accounting records, in terms of auditing, in term of reporting, in terms of managing, in terms of the regulating practices, this government should be clear. I think that element should be something that will help the system [of *waqf* for public expenditure] and something that to [be] worked out seriously.

Meanwhile, Academician G anticipated that the problem of transparency when solved, can even attract non Malaysians to endow:

So they can have these kind of big funds and other contributors from GCC [Gulf Cooperation Council] countries, even other places where they see this kind of endowments [i.e. *waqf* for Malaysian public expenditure] which have contributing very noble purpose, and it has very strong governance, very strong *Shari'ah* compliance, appropriate reporting, and so on so forth.

Academician F on the other hand, just mentioned transparency in passing, "But certainly there will be legal management investment, accounting, this issue will be there".

From this researcher's experience, not all SIRCs are willing to release a complete set of data on *waqf* to the public. When this researcher had asked for quarterly *waqf* data, Government Official D during a personal interview on 28th January 2016 only agreed to

release yearly data. When probed further, Government Official D was reluctant because they had been wrongly accused of corruption before. Government Official D claimed that the accuser was not well versed in the *Shari'ah* of *waqf* so the accusation was baseless.

Regardless, the literature concurs with the findings of the semi structured interview and this researcher's experience. Siraj (2012) noted that only a handful of SIRCs publish annual reports and worse, the published reports contain discrepancies. Discrepancies is a definite taboo for *waqf* financing public expenditure because it can trigger nationwide public distrust which could drive the idea obsolete. In terms of online transparency, Abd Halim and Nurjannah (2016) found that SIRCs provide limited information on the collection and distribution of *waqf* funds. A study conducted by Abu Bakar Manat (2007) also noted a lack of transparency in *waqf* management. As the idea of *waqf* financing public expenditure is relatively new, it is vital and rational that potential *waqif* be exposed to all the required information. Indirectly, a deeper understanding on *waqf* can be fostered.

Zurina et al. (2016) blamed the lack of transparency on the absence of performance measurement framework and monitoring measures for *waqf* management in the law. In the context of *waqf* financing public expenditure that is much significant and bigger in scale, the public could become more sceptical without those two factors at play. Plus there is a lack of accounting standards that can be used by SIRC for *waqf* reporting (Nazifah & Muhammad Firdaus, 2016). WANCORP for instance, prepares statement of accounts following the Malaysian Financial Reporting Standards (MFRS) and International Financial Reporting Standards (IFRS) (WANCORP, 2015). In a case study conducted at an undisclosed SIRC, Nazifah and Muhammad Firdaus (2016) noted the use of Private Entity Reporting Standards (PERS) instead. This difference in reporting standards could garner debates and possibly discrepancies in the *waqf* reporting of public expenditure in the future. The situation is further made worse in the case of *waqf* land where no

systematic registration procedures is in place (Rohayu & Rosli, 2014; Sharifah Zubaidah & Nor Asiah, 2014). As a result, an accurate *waqf* value is difficult to record and may detriment the plan for *waqf* financing public expenditure.

5.3.3   Financing Strategy of Malaysian *Waqf*

Four *waqf* financing strategy were identified from the semi structure interview namely crowdfunding, rental of *waqf* properties, real estate investment, and diversification of investment. Each of these strategies are analysed separately.

According to Government Official B, "We collect all the cash *waqf* and when we reach a certain sufficient amount, we straight away convert the cash *waqf* into immovable property of our choice". Where crowdfunding in Government Official B's organisation is structured around *waqf am,* the crowdfunding in Government Official D's is structured around *waqf khas* (personal interview on 28th January 2016):

Our cash *waqf* is done as such; we first list our projects. Projects 1, 2, 3 4, 5, 6, 7. Assume you have RM100. You want to endow this RM100 into projects made by our SIRC. You can go to our website and select in which project you want to endow.

Crowdfunding simply means raising money from different individuals to finance certain projects. Hence the benefit generated from crowdfunding is often in terms of intangible usage of that project. Government Official A gave one simple example, "We do not sell the house [which is a *waqf*] but we sell the benefits i.e. people can live in that house". Thus, to be able to live in that house is considered as a benefit of *waqf*.

Before sufficient cash *waqf* is pooled, the collected cash *waqf* are saved in a *wakalah* fixed deposit account. This is stated by Government Official B:

Since the collected [cash] *waqf* is not yet high, we only invest it in fixed deposit. [It is] short term meaning we can withdraw anytime … Actually, the most important is the capital [of *waqf*]. If RM10 is invested, we must get back the RM10. So that is the reason why we save in fixed deposit of Islamic banks, *wakalah* deposit [to be exact].

The organisation of Government Official D also did the same to which was said in passing, "It depends on the commitment of that *waqf*. [Specifically] what is the purpose of that *waqf*? It is that collected cash that we deposited in a fixed deposit account". In other words, the collected cash *waqf* are placed in *wakalah* deposit because of its low risk feature, ease of withdrawal, and guaranteed preservation of *waqf* capital. Still, saving cash *waqf* in fixed deposit restricts the cash *waqf* from maximising its return. Academician B for one, opposed this decision:

One of my Master students did research for State Y. She found that 80% of the assets are being used for religious purpose and only 20% are for investment. So in other words to sustain these assets, 20:80 ratio is not good.

As of 10th March 2016, the date this researcher personally interviewed Government Official B, no projects were initiated using the collected cash *waqf* fund because the value is still small. If not address properly, Government Official B's institution will heavily depend on the federal government budget which may as well cause burgeoning expenditure. This is counter intuitive to the idea of this thesis.

However, to be fair, Government Official B's institution has the intention of leveraging on financial securities to finance future public *waqf* projects, "when we have a sizeable fund, millions or billions, we can structure it into *sukuk* and the likes". In fact, the mentioned institution is learning various *waqf* investment modes from other countries, "And apart from Turkey we also refer to a number of countries such as United Arab

Emirates, United Kingdom in regards to cash *waqf,* Saudi Arabia regarding *sukuk,* [and] Singapore in terms of managing *waqf* lands". This effort may perhaps contribute to the development of *waqf* financing federal government expenditures.

SIRCs also derive *waqf* return from rental of *waqf* properties. Government Official A, "We do not sell the house [which is a *waqf*] but we sell the benefits i.e. people can live in that house. For instance, we [give] lease, we [give] rent". The rents are however, extremely cheap and only pay for management fee without increasing further the value of *waqf.* As was informed by Government Official D, "In terms of payment [rent for *waqf* of house], we only ask for RM100 or RM150 a month". This is a classic example given by Çizakça (1998) on disregarding capital pooling which became one of the contributing factor of *waqf*'s downfall in the first place.

Indeed, Syahnaz (2012) as well as Mohd Afendi and Che Zuina (2010) claim that the rental rate for *waqf* properties are far less than the market rate. It is understandable that rents should be cheap so that low income earners can afford the rent. However, the rental rate can still be raise while maintaining a lower market rate. There are also cases of tenants that took advantage of the low rent by sub-renting the unit to another tenant at a higher price (Mohd Afendi & Che Zuina, 2010). Thus, not only the rental income is little, the religious purpose of *waqf* was also forfeited. Imagine that the income of *waqf* for public expenditure sourced from rental payment is also low. The low income may render *waqf* unfitting as the value of public expenditure is in billions of Ringgit.

On the other hand, the company where Industry Expert A originate invests its *mawquf* in a myriad of industries. Plus, when Industry Expert B was asked whether the *mawquf* collected is invested, "Yes, part of our fund is invested in buying real estate properties". Notice that *nazir khas* are willing to take risk in contrast with *nazir am*. It also indicates that the *nazir khas* realises the importance of capital pooling. The most likely reason is

because *nazir khas* has more experienced and knowledge in risk management than *nazir am*. As a result, *nazir khas* were able to sustain and further increase the value of *waqf* collected without depending heavily on the government nor the general public for aid. Undoubtedly, a proactive step such as this will contribute to the value of *waqf* for public expenditure which in turn makes the idea viable. This also subsequently show why lack of human know-how could limit the income arising from *waqf*.

5.3.4   Public Perception on *Waqf*

As was claimed by Government Official D, poor public knowledge on *waqf* is a crucial issue, "The public understanding on *waqf* is the biggest challenge". During the interview, Government Official D gave two such examples. The first example is:

Waqif tend to view *waqf* of mosque as the best form of *waqf*. However, in that village, two to three mosques sites are already in place. Do we as a trustee should build another mosque in that village? The village only has twenty houses. [Thus] it is not practical and is not even permissible from the *Shari'ah* standpoint. So we did not build another mosque.

Academician B concurred with this, "And I think the awareness is lacking because based on our studies, we found that Muslims think that *waqf* is mostly for religious purposes".

It is a shame that Muslims do not realise the significance of *waqf* and its relation to economy in history. This kind of thought process supresses the far reaching benefits of *waqf* and its potential application including that of *waqf* financing public expenditure. As a result from this, little *waqf* endowments were made presently for pure and mixed public goods. As has been alluded earlier in this chapter, the root cause for this is Western

imperialism (Rohayu & Razali, 2009; Razali, 2015) that had separated *waqf* from economics. The tradition of endowing *waqf* outside of religious purposes thus steadily diminishes. However to be fair, there are efforts been made to increase the awareness of *waqf* in Malaysia. For instance, Mustapahayuddin and Noor Hani (2014) claimed that the SIRC of Johor has made an effort to promote awareness using instruments of mass media such as through internet, flyers, radio, newspapers, television, and others.

The second example given by Government Official D is:

We already mention there are seven projects. If the *waqif* state that his or her endowment is for Project 1, then I [SIRC] cannot use his or her endowment on other projects or anything else. [It is strictly] not allowed. His or her *sighah* is for that [i.e. Project 1]. So I [SIRC] must comply. Hence a related issue might be, "ustaz, to get RM10 million for that project takes how long a time?" Maybe a year, maybe three years, maybe six years, maybe seven years. It depends on the *waqf* demand.

What Government Official D was intending to say is, the public had doubts toward the SIRC for not developing *waqf* projects within a certain time frame acceptable to them. This doubt is however baseless because it is incumbent upon SIRC as the trustee to spend the available *waqf* fund only on projects selected by the *waqif*. In addition, SIRC will not be able to proceed with the mentioned project development if the total fund needed is not yet sufficient. In the context of *waqf* financing public expenditure, members of the public that do not possess adequate knowledge on *waqf* will grow suspicious hence disrupting the idea at the early stages of implementation. Should this happen, *waqf* financing public expenditure will not be able to reach its zenith.

Malaysia is a multi-ethnic country comprising of people from various religious backgrounds. Based on this fact, Academician B stressed that the non-Muslims must also understand the concept of *waqf*:

> For us, there has a bearing in this world and hereafter. If you [the non Muslims] are contributing it is just for the sake of humanity. So in other words, their contribution should not affect the policy, the direction, all the structure of *waqf*, then there is no harm. They can contribute for humanity.

This statement made by Academician B is not a prejudice statement. The interviewee is simply trying to get a point across. Muslims already know in principle that the basis for *waqf* endowment is goodness hence must not be made due to any ulterior motives. On a side note, this thesis already recognised the allegations of Baer (1997) and Peri (1992) regarding mismanagement by Muslims themselves in Section 2.3.1. Non Muslims on the other hand, might not understand this in principle and assume that *waqf* is a mere fiscal tool. Connecting back to the application of *waqf* for public expenditure, lack of realisation of the basis for goodness in *waqf* may deter non Muslims from endowing *waqf*.

Besides the issue of *waqf* understanding, Malaysians have this attitude of depending heavily on the government to provide for their need. According to Academician F:

> One of the big challenges you'll face in Malaysia now is whenever you ask people to make *waqf* of certain thing, they will say but that is government's role. Trying to get people to give money to universities, they'll say this is government's role.

An indirect outcome of this is the possibility of not wanting to endow *waqf* for public goods, mixed public goods, and other related social services. This would make the idea of *waqf* for public expenditure void for Malaysia.

5.4   Conclusion

Chapter 5 had provided evidence for the applicability of *waqf* financing public expenditures. Arguments were provided from the *Shari'ah* standpoint, historical application, and present indication. *Waqf* financing public expenditure is permissible from the *Shari'ah* standpoint and had been successfully applied to some extent in history. In addition, the Malaysian federal government is supportive of *waqf* and showed indication to employ *waqf* in such manner. This thus answers RQ one.

Since the idea of *waqf* financing public expenditure is relatively new, various interconnected issues were identified. In legal terms, majority of the state laws do not contain stipulation that can give permission to private sector to manage *waqf*. This may be deemed idiosyncratic for *waqf* financing public expenditure because SIRC will need the skills and experience that private sector possesses to implement the idea successfully. In addition, most SIRCs do not promulgate specific *waqf* enactment which can cause confusion in the execution and management of *waqf* for public expenditure. Another intuitive issue that was mentioned is court settlement. *Waqf* disputes are resolved in *Shari'ah* courts but public expenditure does not.

In management terms, the issues identified were human resource problems, bureaucracy, and lack of transparency. Shortage in experts together with the existing broad job scope will cause the execution of *waqf* for public expenditure to be done haphazardly. Meanwhile, the public views bureaucracy and the lack of transparency as a weakness of *waqf* management which will deter them from endowing *waqf* for public expenditure. Analysis of the semi structured interview also showed evidence on the employment of unprofitable financing strategies. Without strategies that can optimise return, *waqf* for public expenditure may not be sustainable in the long run. Lastly,

negative public views and low comprehension on *waqf* may make the idea of *waqf* for

public expenditure undesirable. RQ 2 is thus answered and RO 1 is accomplished.

CHAPTER 6: FINANCING SELECTED COMPONENTS OF FEDERAL GOVERNMENT EXPENDITURES

6.1 Introduction

It has been established in Chapter 5 that *waqf* financing certain Malaysian federal government expenditures is doable. Issues that could arise from its implementation has also been identified in the same chapter. This chapter will focus on those issues that directly concern with the development of a model for *waqf* financing federal government expenditures which are *waqif, mawquf, waqf* trustee, financing strategy, and *mawquf 'alaih*. These components are the same in *waqf* models reviewed in Section 2.4.3 (Figures 2.2 - 2.5). In addition, this chapter will also determine some of the data needed to be factored in the DSGE model. The specific data are the form of *mawquf* and its financing strategy.

This chapter presents the findings of RO 2 that corresponds to RQ 3. To reiterate, RO 2 is "To come out with a model of *waqf* financing certain components of federal government expenditures in Malaysia", while RQ 3 is "How can *waqf* finance certain components of Malaysian federal government expenditures?" Hence, the purpose of Chapter 6 is to come out with a model that will provide the mechanism for *waqf* to finance public expenditures. The findings of this chapter also help shape the theoretical model presented earlier in Section 4.5.1.

Basically, Chapter 6 is organised as follows. Section 6.2 presents the themes gathered from the interviewees' transcripts that tackle the *waqf* issues identified in Chapter 5. Using these solutions, the model is then built in section 6.3. Lastly, a conclusion is presented in Section 6.4.

6.2   Addressing the Issues of Malaysian *Waqf*

Three themes materialised pertaining to the issues and solutions for *waqf* of public goods and other social services in Malaysia. These themes are *waqf* laws, *waqf* management, and *waqf* financing strategy. A cursory look suggests that the latter two are important factors for the model's practical operation. *Waqf* laws, on the other hand, give permission for the model to operate. Thus, these themes are highly relevant to the model building of *waqf* for financing certain federal government expenditures. Each of these themes are argued critically in the subsequent sections.

6.2.1   Partial Centralisation of *Waqf* Laws

To recap from Section 5.2.1, SIRC is the sole trustee of *waqf* in Malaysia which means that SIRC will also be the trustee for *waqf* financing public expenditure. In addition, different states have different *waqf* laws. Since *waqf* financing public expenditures concerns the whole of Malaysia and by extension all states, there is a question of SIRCs capability and different state laws' practicality. Thus, this section relates to the *waqf* trustee component of the model.

To determine the best solution for the stated issues, answers given by interviewees are scrutinised. Six subthemes have emerged. The first subtheme is that *waqf* should be made completely independent from the SIRCs so that the Malaysian public can initiate *waqf* according to his or her own terms. In other words, total law amendment must be made to abolish SIRCs as the sole trustee of *waqf* in Malaysia. This is the belief of Academician A:

So, the *Deen* council (SIRC) are great impediment of *awqaf* in Malaysia and the management of *awqaf* should be freed, determined only by the founder of the *waqf*…

add *waqf* independent of decree from the government. Like any other NGOs [non-governmental organisation].

This first subtheme agrees with Çizakça (2000) who considered appointing SIRCs as the sole trustee causes decline in *waqf* creation, "Under these conditions of extreme centralisation, no wonder the Muslims in Malaysia refuse to endow their properties as *waqf*" (p.123). Kahf (2014) is also cynical, "It does not take a gifted genius to ascertain that the perception of Islamic *awqaf* as a part of the public sector is completely incorrect" (p.205). Analysing closely, these studies share one similar reason for their stand; government inefficiency and corruption. Kahf (2014) claimed that government are infamous for mismanagement of economic activity, while Çizakça (2000) stated the unfairness of making SIRC as the sole trustee of *waqf* when it is tradition for founders to freely appoint managers.

It is an undeniable fact that making *waqf* independent reduces much bureaucracy. Land can simply be endowed without subjecting it to evaluation, founders have more liberty to set the terms for *waqf*, and most importantly, founders will not have to go through SIRC. As the overall matter of *waqf* management is on the hands of the founder, there will be more motivation for the public to endow *waqf*. An indirect result from this is the formation of *waqf* for public goods and other social services like during the Ottoman Empire. On top of that, the tradition of *waqf* as a pure societal instrument can be revived.

However, making *waqf* independent actually increases the potential for *waqf* to be lost, at least in the case of Malaysia. Government Official B pointed out that:

Meaning (s)he endows *waqf* for the family's use. We won't stop it. It's just to avoid corruption, misuse, or family feud, it is better that the said *waqf* be registered with the SIRC. When it is registered, should there be any claim in court, the court will favour

SIRC because that *waqf* has been registered. So, in state statutes it has been detailed that SIRC is the beneficial owner of state *waqf* lands.

Academician A asserted that the above can be avoided by erecting another law to safeguard *waqf*:

We need a law of *waqf* to regulate its establishment, to regulate its management, to control, or to subject rather its management to very strong auditing, that maintain the integrity of the property and its use or its objective that avoids corruption...

This assertion of converting *waqf* into a legal entity is supported by (Kahf, 2014).

Abolishing the stipulation on SIRCs as the sole trustee of *waqf* impact other stipulations in the state statute too. Taking example from *Wakaf* (State of Selangor) Enactment 2015, Section 4(1)(b) and 4(1)(c) that gives the power to SIRC of Selangor to allow other parties to administrate *waqf* may be nullified and also Section 5(1) that states all *mawquf* is vested in the SIRC may be annulled. Similarly, Section 43 that gives jurisdiction to the SIRC to make regulations on *waqf* could be invalidated. In other words, the first subtheme calls for the abolishment of many existing *waqf* laws and the enactment of substantial new *waqf* laws. This will require an unprecedented amount of time to take place. Even if this feat might be achieved, the Malaysian public might not even choose to endow *waqf* for the purposes of public goods and social services. In the case that they do, there will be a possibility of oversupplying certain goods and a deficit on others. This is certainly not a favourable scenario for countrywide provision of these goods. Besides, Academician C claimed that making *waqf* independent is a lost cause as it concerns the sensitivities of Rulers:

Yes indeed. I myself do not agree [with SIRCs as the sole trustees of *waqf*]. I did suggest for a law amendment during a research in 2005 but SIRCs do not agree due to

154

the power of Rulers and others". Again, duly take note that SIRCs act under the Rulers' power.

The second subtheme calls for a complete centralisation of *waqf* law. According to Government Official C, "If we can centralise *waqf*, knowledge sharing can easily be fostered between different states and *waqf* for education and infrastructure for example, can easily be provided nationwide".

Centralisation of *waqf* law means that there will be only one Act that governs Malaysian *waqf* under the Federal Law. In the case of *waqf* financing federal government expenditure, this Act ease the pooling of *mawquf* under a single administrator and the nationwide dissemination of the *mawquf*'s benefit. Inadvertently, bureaucracy will be greatly reduced because there is only one governing law. Besides, the federal government can easily name the goods and services that require the funding of *waqf*. This eliminates the problem of oversupply of certain items and deficit of other items that the first subtheme has. Academician B had emphasised on this matter:

Tax is given by the public so the government use it to finance its expenditure. In other words, when we give tax to the government, it is up to the government [to decide] how to use the tax. But usually in *waqf*, the deeds is specified, it's very specific. In other words, there is something which is identified by the government, [for example] the government says we need roads, the government says we need parks.

If the government does not name the expenditure items required for *waqf* funding, founders might view *waqf* like a voluntary tax which robs the spirit of goodness embodied in it. An in-depth discussion on *waqf* deed will be provided in Section 6.2.2.2.

Attempt for centralisation did occur through the suggestion to instate Federal Territories *Waqf* Act 12 years ago (Sharifah Zubaidah, 2016). Should this materialise, the Act will nullify state *waqf* laws as per contained in Article 75 of the Federal Constitution. However, Federal Territories *Waqf* Act did not come into fruition. Sharifah Zubaidah (2016) alluded that it is because of the unwillingness from all states and royal institutions to accept the Act. After all, Article 74(2) and Article 74(3) of the Federal Constitution permit states to determine its own decision on *waqf* laws. This indirectly concerns the sensitivities of the royal institution.

Along the same line, Academician E also held the same opinion but through the uniformity of *waqf* law:

The federal government have the urge to form some kind of uniformity so the benefit can be enjoyed from one state to another state. I think this is another issue that has to [be] worked out with the Ruler as well as the state authority.

Indeed, uniformity in *waqf* law will promote cheaper transaction costs, further transparency, positive public perception, and lesser bureaucracy (Sharifah Zubaidah & Nor Asiah, 2014; Sharifah Zubaidah, 2016). Taking example from Sharifah Zubaidah (2016), a *waqif* might reside in a different state and had endowed *waqf* in another state while the managers of said *waqf* could be operating in a different state. With the dissimilarities of *waqf* laws between these three states, one can imagine how complicated the management of *waqf* would be. Hence, in the case of this thesis, the current inconsistent law could complicate the process of pooling *waqf* endowed by founders from different states to a manager in another state before distributing the benefits from that *mawquf* to the *mawquf alaih* nationwide. Hence, administering *waqf* for financing public expenditure will be carried out with less complexity and more transparency when all state laws are similar.

In reality, the process of attaining uniformity has long been initiated. Attempt for uniformity was carried out by JAWHAR through the publication of the Manual of *Wakaf* Legislation Model Management *(Manual Pengurusan Model Perundangan Wakaf)* in 2008 hoping that states would copy the model of uniformed *waqf* bill presented in this manual. The bill contains stipulations on powers and responsibilities of Majlis, formation of *waqf*, *mawquf*, *mawquf 'alaih*, appointment of registrar of *waqf* and other officer, *waqf* committee management, *waqf* fund, invalid *waqf*, wrongdoings and penalty, enforcement and investigation, general provision, transitional provision, and miscellaneous. Despite this effort, only Perak had copied the suggested uniformed *waqf* bill while other states are hesitant (Sharifah Zubaidah, 2016). However, the states that had introduced *waqf* enactments and rules do contain roughly half of the stipulations outlined in the suggested uniformed *waqf* bill.

Meanwhile, the third subtheme states that SIRCs only need to manage religious *waqf* and private *waqf,* while philanthropic *waqf* could be centralised. Definitions of these *waqf* categorisation are given by Kahf (2014) and Mohammed Obaidullah (2008) in Section 2.2.4. In the words of Academician G:

> The traditional *waqf* can be under the SIRCs; but the new form of cash *waqf* models which is more driven by finance, economics, and government initiatives that serves some economic sectors for the government cannot be under the purview of the SIRCs.

Basically, this third subtheme maintains the role of SIRCs as the sole trustees for religious and private *waqf* but not for philanthropic *waqf*. This is because *waqf* for financing expenditure is the subset definition of philanthropic *waqf*. Hence, *waqf* for public expenditure may as well be instituted according to other Items in the Federal List. For instance, Item 2 for defence, Item 10 for communications and transport, Item 13 for education, and others. Indirectly, both Rulers' sensitivities and development for *waqf*

financing federal government expenditure are greatly considered. Comparing further with the previous two subthemes, this option of partial centralisation is by far the most practical and doable. It does not completely dismiss SIRC as the trustee of *waqf* and the right of states to promulgate their own *waqf* laws. Another indirect consequence of excluding SIRC to manage philanthropic *waqf* is that it addresses the shortage of manpower and broad job scope at SIRCs. Pursuant to this, categorisation of *waqf* should be redefined in state laws and include SIRC as the trustee for religious and private *waqf*.

On the other hand, the law of *waqf* for financing public expenditure can be promulgated in the suggested Federal Territories *Waqf* Act with due consideration of the Items in the Federal List. This is similar with the IBA (1983) that had considered Item 7 and Item 8 of the Federal List. Reconciling this context and the current administration of *waqf* in Malaysia, YWM is the most legible body to become the trustees of philanthropic *waqf*. After all, YWM is the national *waqf* entity of Malaysia. Figure 6.1 illustrates the suggested laws and trustees for the different types of *waqf*. Note that philanthropic *waqf* corresponds to *waqf* for financing certain federal government expenditures.
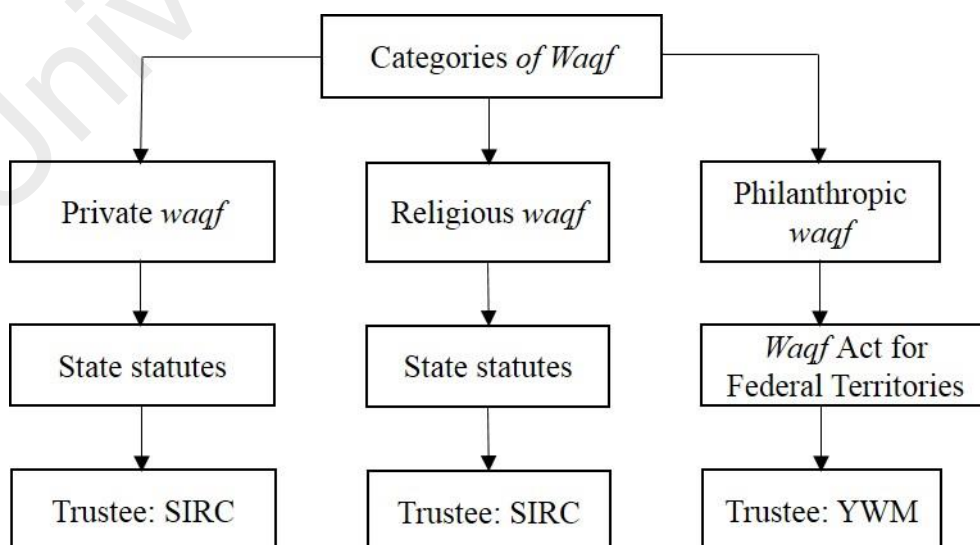
Figure 6.1: Suggested Trustees of Waqf in Malaysia

Now if partial centralisation were to put in place, what of the *nazir khas* such as public universities and corporate *waqf* bodies like WANCORP? *Waqf* for education in public universities are essentially *waqf* for public expenditure and some beneficiaries of WANCORP are for social services. Should they continue to assume their role as *nazir khas* or be subjected under YWM's management? In this case, YWM can acquire the role of *nazir 'am* for these *awqaf* just like SIRCs were and they remain as *nazir khas*. In fact, YWM should be given the authority to give permission to other parties to manage their own *waqf* of public goods. These are similar stipulations in Section 4(1)(b) and Section 4(1)(c) from *Wakaf* (State of Selangor) Enactment 2015. Therefore, these are examples of provision that should be outlined in the Federal Territories *Waqf* Act.

The fourth subtheme had also argued for partial centralisation but in accordance to the *waqf* categorisation most common in Malaysia. As denoted by Academician D during an email interview on 25th March 2016, "… centralised for the public *waqf* [*wakaf 'am*] and decentralised for the specific *waqf* [*wakaf khas*] which is lacking in Malaysia at the present time". In other words, *waqf* for financing expenditures is given a subset definition of *wakaf 'am*. This recommendation which also takes into account the Rulers' sensitivities and state laws to some extent is practical and doable, allows SIRC to still be a trustee for *wakaf khas*, as well as it addresses the shortage of manpower and broad job scope of SIRC. In addition, *wakaf khas* such as public universities and corporate *waqf* bodies managed by a *nazir khas* may still be under the supervision of SIRC as the *nazir 'am*. Comparing further with the third subtheme, the fourth subtheme possessed another advantage. It requires lesser change in the state laws as the definition of *wakaf 'am* and *wakaf khas* are already incorporated in Wakaf (State of Selangor) Enactment 2015, Wakaf (State of Malacca) Enactment 2005, Wakaf (Negeri Sembilan) Enactment 2005, and Wakaf (Perak) Enactment 2015.

Nonetheless, the very definition of *wakaf 'am* excludes documentation of precise *waqf* deeds. Recall that in Section 2.2.4 that *wakaf 'am* is founded for the purpose of providing social needs and economic services in general without being specific. Thus, it is counterintuitive to the recommendation of Academician B who valued and recommended specific *waqf* purposes. As has been elaborated in the previous chapter, founders might then view *waqf* as a form of voluntary tax. Academician F had earlier stated that Malaysians have the tendency to depend heavily on the government so to make *waqf* for financing expenditures appear to be like a form of voluntary tax is counterproductive. Besides, Duncan (2004) claimed that donors are more willing to donate for a specific good rather than across multiple goods.

The fifth subtheme is to allow the state *waqf* laws to remain as they are but include stipulations that permit additional role from the federal government. For instance, Government Official A stated that:

The current legal framework in Malaysia can be employed. But the federal government must have more vision [in it], the federal government must acquire more role in the legislation for that purpose [i.e *waqf* financing public expenditure].

Now how exactly can federal government acquire more authority in *waqf* so that *waqf* financing public expenditure can take place? The most likely solution is that the federal government should be given more authority to decide the projects to be built using *waqf 'am* funds. Similarly, the federal government can decide beforehand the projects for *waqf khas* too. This way, the federal government may supply the public goods needed through *waqf* and reducing its expenditure while the SIRC's role as the sole trustee is retained.

A cursory look on this suggestion may seem probable due to the fact that JAWHAR is currently given authority to decide on the types of projects to be developed on *waqf* lands.

However, the development of *waqf* land is a form of *waqf irsod* where the federal government used its own revenue to finance the projects. Basically, the projects' *waqif* is the federal government and as a *waqif* the federal government do have the right to make its own decision. This had included the appointment of YWM as the trustee. On the other hand, the fund of *waqf 'am* and *waqf khas* comes from the general public and these funds are under the management of SIRC. Thus, the founders are the general public while the trustee is SIRC. Should the federal government have the final say, this may lead some to assume that the federal government is exerting unwanted authority. Federal law and state law may as well be indistinct. Transparency then becomes heightened. Disagreements may then happen which subdues the potential of *waqf* financing federal government expenditure. Ultimately, the case of subtheme three will occur.

Lastly, the sixth subtheme accepts the existing state *waqf* laws without needing any additional stipulations. Hence, this solution requires that the mechanism of *waqf* financing federal government expenditure to operate under existing *waqf* laws. As was stressed by Academician C, "Actually *waqf* could be used for various application provided that all the *hukum* and all the laws for that state concern is observed. That's very important". When inquired whether SIRC is proficient to be the trustee of *waqf* for public expenditure, Industry Expert A had answered, "In my opinion, if it concerns state X, I would say yes because there is endorsement from our leadership". Besides, suggestion of Industry Expert B can be employed in the case of amateurish SIRCs that is "… strategic collaboration between SIRCs and financial institution".

There is no doubt that Malaysian *waqf* laws are improving. For instance, founders can ask permission at SIRCs to collect and manage own *waqf* fund like the Al-Abrar *Waqf* Fund and other universities. Financial securities like company shares and *sukuk* are accepted as *mawquf* which led to the founding of corporate *waqf* such as WANCORP. In

the context of this thesis, the federal government may seek permission from SIRC to collect and manage *waqf* for financing expenditures.

However, the permission is only valid in that state. Recall that not all states have these stipulations in their states statutes. Hence, the states that cannot by law grant permission to the federal government to manage *waqf* fund will be deprived from the benefits of the *waqf* in question. Example of these states are Kelantan, Pahang, Perlis, and Kedah that also have low mean monthly household income (DOSM, 2015). One of the significance of this thesis is that Malaysians' welfares are still taken care of despite the attempt to reduce federal government debt. Therefore, to retain the existing *waqf* laws without consideration of the low-income states invalidates the significance of this thesis.

Of course, the suggestion by Industry Expert B may be applied, "Members of the states' Fatwa Committee have to work together with *waqf* managers to identify issues that need fatwa for execution". Meaning, the federal government may cooperate with the states' Fatwa Committee and ask for a decision to use *waqf 'am* funds and be given authority in selecting *waqf khas* projects. Recall that YWM is a federal government *waqf* entity, hence, can be viewed as a *waqf* manager. Note that this suggestion by Industry Expert B is simultaneously addressing the issue of lacking progressive fatwa. Still and if the state fatwas allow for federal government participation, ultimate promulgation in law will highly likely occur. This means that subtheme three again becomes the most practical application out of the six subthemes.

6.2.2   Enhancing *Waqf* Management

As was deliberated in section 5.2.2, the issue of *waqf* management for financing public expenditure revolves on transparency, human resource, and bureaucracy.

However, the suitable *mawquf* for this particular implementation of *waqf* is cash (see Section 6.2.3). Since bureaucracy mainly involves *waqf* lands, this issue will not be addressed. As will be discussed in Section 6.2.3.1, cash is the most suitable *mawquf* for the application of *waqf* in question. Hence, only solutions to the issue of transparency and human resource are given focus. Just to be clear, transparency relates to *waqif* and human resource relates to *waqf* trustee.

Three subthemes emerged from the interview transcripts. The subthemes are *waqf* report publications, documentation of *waqf* deed, and human resource empowerment. These are analysed in order. Note that the management of religious and private *waqf* that remain under SIRCs that was proposed in Section 6.2.1 is irrelevant to this thesis.

6.2.2.1 Publication of *Waqf* Reports

Interviewees stated that lack of transparency is an obstacle to *waqf* financing public expenditure. Literature had also pointed out that accounting and reporting of current *waqf* activities in Malaysia are imperfect (Abu Bakar Manat, 2007; Siraj, 2012; Abd Halim & Nurjannah, 2016). It is crucial that potential founders are given access to *waqf* fund activities because the idea of *waqf* financing public expenditure is relatively new. This indirectly educates them on the *waqf* application and promotes public confidence which indirectly addresses the issue of public perception outlined in Section 5.2.4. Hence, *waqf* will no longer be perceived as an archaic instrument suitable for pure religious purposes only, but is in fact a versatile instrument capable to also discharge economic duties. Chances are the value of *waqf* for financing federal expenditure may rise as a result.

Academicians G and E respectively pointed out the obvious solution to transparency which is publication of report:

So, they can have these kind of big funds and other contributors from GCC country, even other places where they see this kind of endowments [i.e. *waqf* for Malaysian public expenditure] which have contributing for very noble purpose, and it has very strong governance, very strong *Shari'ah* compliance, appropriate reporting, and so on so forth.

… the government should have very clear governance of this *waqf* in terms of for example, the accounting records, in terms of auditing, in terms of reporting… I think that element should be something that will help the system [of *waqf* for public expenditure] and something that to [be] worked out seriously.

Academician H also recognises this, "The second thing is, I agree that transparency in reporting is needed …".

In an attempt to assist SIRCs with *waqf* reporting, JAWHAR had published *Manual Pengurusan Perakaunan Wakaf* or the Manual of *Wakaf* Accounting Management in 2009. In this manual, JAWHAR had laid out in detail among others, the relevant laws pertaining to *waqf* accounting, method to *waqf* accounting, and format of *waqf* financial statements. Basically, the manual contains a set of best practices for *waqf* accounting that SIRCs are encouraged to follow. Adding on to this, *waqf* for financing public expenditure should include details on the *waqf* concept, *waqf* activities, governing *Shari'ah* and Malaysian laws, as well as the management of the *waqf* in its reports.

Unlike most *nazir 'am*, *nazir khas* do report on their *waqf* activities. Take example from WANCORP and BMMB. WANCORP publishes annual reports detailing among others the value of JCORP's *waqf* of shares, dividend obtained from investment of *waqf* of shares, and allotment of benefits to recipients from the dividend. Statement of accounts were also prepared according to the MFRS, IFRS, and Companies Act 1965. In fact, the

format that WANCORP adopted for reporting resembles the Manual of *Wakaf* Accounting Management. Aside from reporting, WANCORP is also subjected to auditing. On the other hand, BMMB publishes quarterly reports only on the value of *waqf* fund available and amount allocated to *waqf* beneficiaries. Thus, BMMB's reporting on *waqf* is not as thorough as WANCORP. It is the opinion of this researcher that the suggested trustee of philanthropic *waqf*, YWM, should at least follow the method of WANCORP's *waqf* reporting.

Later in Section 6.2.3.2, YWM's collaboration with an Islamic unit trust firm will be reasoned. It is the norm for Islamic unit trust firm to publish annual and intermittent reports. Therefore, YWM can also work together with the firm to produce a cohesive report on amount of cash *waqf* collection and distribution on one hand, and return from cash *waqf* investment on the other.

6.2.2.2 Revivification of *Waqf* Deed

Academician B had stressed on the importance of *waqf* deed which precisely documents the will of the *waqif*. This include specification on *mawquf 'alaih* or purpose of *waqf*. To reiterate, specification of *waqf* deed may increase the possibility of Malaysians to become founders for *waqf* financing public expenditure. It helps the *waqf* to retain its spirit as a third sector instrument that promotes goodness instead of a voluntary tax that disguise itself as a third sector instrument. To save cost, reduce bureaucracy, and promote easy understanding, the *waqf* deed should be formatted into a form and filled out online by founders at the official website of YWM. When the form is complete, then a *waqf* deed is then generated.

The surviving copy of Ahmed Pasa's *waqfiyah* possessed by the Free Library of Philadelphia sheds light on the information that has to contain in a *waqf* deed. The information are certification and testimony of witnesses, a prologue, inventory on the *mawquf* and beneficiaries, as well as manner of *waqf* administration (Turgut, 1981). On the other hand, current *waqf* records by MUIS are more concise detailing on the trustees, beneficiaries, *waqif,* and *mawquf* as well as the way income from *waqf* is divided between the beneficiaries and management (MUIS, n.d.). In addition, Mohsin (2009) recommended to also include the ten stipulations for *waqf* endowment namely *ziyadah* and *nuqsan*, *idkal* and *ikhraj*, *i'ta'* and *hirman*, *taghyir* and *tabdil*, as well as *istibdal* and *ibdal*. However, as has been mentioned in Section 2.2.3, it is not mandatory for the last two stipulations to be included as both can still be carried out without founder's consent.

In the case of *waqf* financing public expenditure, the trustee (YWM), *mawquf* and its investment method (see Section 6.2.3) are already predetermined. Income from *waqf* is not divided between beneficiaries and management (more detail in Section 6.2.3.2). YWM must consider with due diligence the appropriate beneficiaries and form them into multiple choices so that the public may select the option(s) they most desire. The first seven stipulations from the ten stipulations for *waqf* creation may also be included in the form of multiple choices. Note that *tabdil* is not included in the *waqf* deed as the form of *mawquf* can never be changed. Lastly, it is appropriate that all five pillars of *waqf* are outlined in the *waqf* deed. Hence, the comprising items for the *waqf* deed are as below:

1. Name of *waqif*

2. Purpose of *waqf* or the *mawquf 'alaih*

3. Investment strategy of *mawquf*

4. Option for *ziyadah* and *nuqsan*

5. Option for *idkal* and *ikhraj*

6. Option for *i'ta'* and *hirman*

7. Option for *taghyir* and *tabdil*

8. *Sighah*

Purpose of *waqf* can be designed by referring to the components of Malaysian federal government expenditures that we had determined in Chapter 3. To reiterate, the components are subsidies and all the federal government development expenditure except for general administration. There are 11 components in total. It is however important, as mentioned earlier on, to further clarify the end recipient or beneficiaries of *waqf*. In other words, for each component of the federal government expenditure, there are many *waqf* deeds in accordance to different end beneficiaries. This is illustrated simply in Figure 6.2. To recap from Section 3.2 of Chapter 3 for the category of subsidies, these items are cash assistance, educational assistance, incentives for farmers and fishermen, cooking oil subsidy, toll compensation, and fuel subsidies. For defence and security, these items are as stated in the Malaysian Economics Report of 2015/2016 which include improvement in surveillance, military equipment, and upgrading of forensic system. For trade and industry, the specified beneficiaries include entrepreneurship development programmes, palm oil industrial cluster, eco-tourism projects, and other projects that promote economic growth.
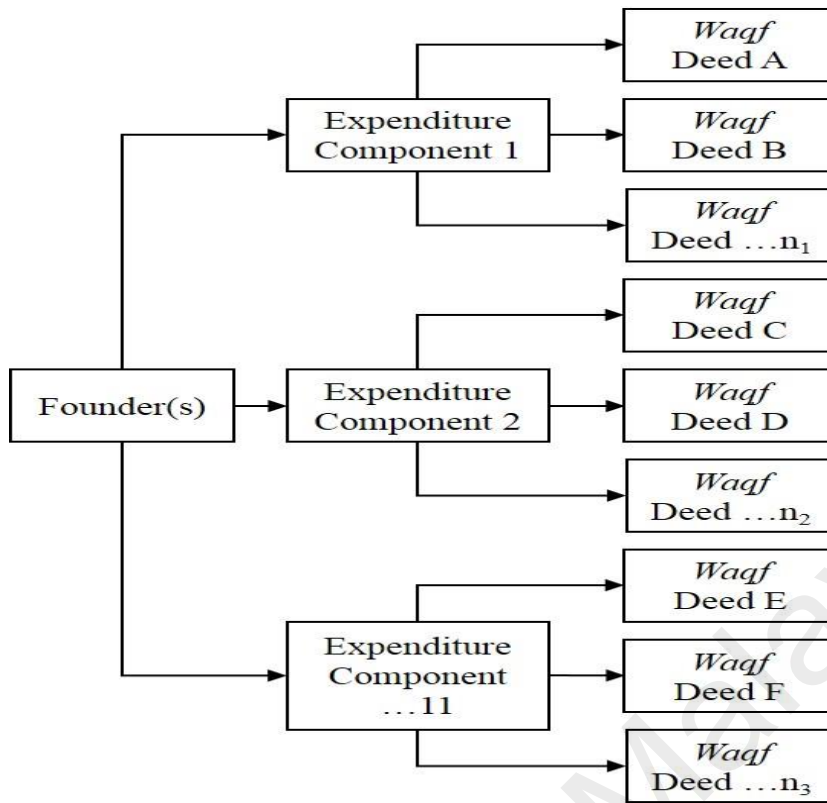
Figure 6.2: *Waqf* **Deeds for each Federal Government Expenditure Components**

Meanwhile, according to the Malaysian Economics Report of 2010/2011, the specific beneficiaries for agriculture and rural development includes projects like irrigation, aquaculture, flood mitigation projects in rural areas, and others. Meanwhile, the specific beneficiaries for transport consists of construction, maintenance, and upgrade of roads, bridges, railways, ports, and airports. As for public utilities, the specific beneficiaries are water supply, electric supply, and sewerage system. Others include miscellaneous items that are associated with the economic sector. On the other hand, the specific beneficiaries for education consists of university buildings expansion, construction of schools and training institutes, equipment upgrading, enhance skills training, and research programmes among others. Housing is for the middle and lower income group.

Health is for additional building of hospitals, ambulance procurement, mobile clinics provision, and others. Lastly for social and community services, the purpose of *waqf*

involve expenditure in upgrading and building parks and recreational facilities, solid waste management, welfare services for the elderly and other vulnerable groups, flood prevention projects, rehabilitating rivers, fire-fighting services, and similar others. However, bear in mind that the specific beneficiaries are not static but constantly changing depending on the needs of the public. Therefore, the specific beneficiaries that were mentioned although real, play more of an illustrative role in this thesis to explain how specific beneficiaries can be stated in the *waqf* deed.

Now the option for *ziyadah* and *nuqsan* relate to founders that endow *waqf* for more than one expenditure item. These founders should be given the opportunity to accept or reject this option. If they do accept, the founders must state the maximum percentage of change that they would allow. On the other hand, the rest of the stipulations relate to all founders. The option of *idkal* and *ikhraj* if agreed, must further be attached with another two options. One, to let YWM as a trustee to make the decision on behalf of the founders or two, the founders choose to make their own decision. Thus, YWM must especially inform founders of the second option when the initial beneficiaries are not in need anymore and present to them another set of options containing other potential beneficiaries that are in dire need. *I'ta'* and *hirman* should also be given further two options if accepted. The further two options are either to allow YWM to carry out the mentioned two stipulations, or the founders themselves notify YWM when they choose to do so. On the other hand, *taghyir* is exclusively the rights of *waqif*. The *waqif* should be given the right to exercise it wherever (s)he wants. Of course, YWM should be given the right for say, three processing days to carry out the founders' will.

6.2.2.3 Human Resource Empowerment

The chief issue of human resource was the lack of knowledge in *muamalah*, especially in terms of *waqf* financing and capital pooling. In regard to this, Industry Expert B recommended to adopt "… strategic collaboration between SIRCs and financial institution". In the case of this thesis, YWM should also adopt a strategic collaboration with a financial institution, specifically with an Islamic unit trust firm. The reason being is *waqf* for public expenditure will be invested in Islamic unit trust fund as is thought out in Section 6.2.3.2. The collaboration brings in experts in risk management and portfolio fund management. It also lessens the broad job scope that YWM might face.

6.2.3 Adopt Innovative *Waqf* Investment Method

It is crucial that *waqf* financing expenditures adopt investment method to take consideration of capital pooling and the perpetuity principle of *waqf*. Note that innovative *waqf* investment method relates to *mawquf* hence important to be discussed in this chapter.

Before the discussion can formally begin, *mawquf* that is most suited for financing expenditure has to be determined first. This is done in Section 6.2.3.1 where three subthemes were identified from the interviewees' transcript; cash, land, and company shares. Then Section 6.2.3.2 details on the suitable *waqf* investment method.

6.2.3.1 Cash as Mawquf

Answers from the interviewees can be categorised into three namely *waqf* land, *waqf* of shares, and cash *waqf*. Thus, this section compares and contrasts between the three to add precision and confidence to the final decision.

Government Official A during a personal interview on 7th June 2016 said:

All the *waqf* lands that we have right now, the federal government can help to develop. That is one of the ways that the federal government can help SIRC. This is because *waqf* lands have potential. It has potential because if we can develop these lands, the federal government will be less burdened to elevate the *ummah*'s (Muslim's) economy.

The abundance of Malaysian *waqf* land was also stated by Mohamad Zaim et al. (2015). With the availability of *waqf* lands, *waqf* contribution from the public to finance expenditure is almost unnecessary.

However, recall that there are many issues surrounding laws on *waqf* lands that were discussed in Section 5.2.1. To reiterate, these issues include no tax incentive entitlement, bureaucracy in converting land to *waqf*, lack of specific stipulation regarding *waqf* lands in the NLC, poor registration of *waqf* lands, and others. The myriad issues of *waqf* land were also attested by Rohayu and Rosli (2014), Sharifah Zubaidah and Nor Asiah (2014), as well as Sharifah Zubaidah (2016). Hence to use *waqf* land as *mawquf* only puts another layer of step required to realise *waqf* for expenditure. This will lengthen the process of instating the *waqf*.

On the contrary, Industry Expert A is of the opinion that *waqf* of shares is the way forward for *waqf* financing expenditures, "In my opinion, if we want to further develop *waqf* [for public expenditure], maybe there should be a ministry that manages *waqf* of shares". To reiterate, *waqf* of shares is the shares of firms or the firms' existing shares committed for *waqf* (Siti Mashitoh, 2011). In other words, individuals that own company shares are able to endow *waqf*. Public listed companies can also allocate a sum of shares for *waqf* financing public expenditures instead of selling them in the capital market. Dividend from these shares can then be used to finance for welfare time and again. This

is actually the concept of corporate *waqf* as defined by Mohsin (2014) that the federal government is pushing forward.

Nevertheless, similar to land, equities are not possessed by every individual. This hinders a sizable number of people from endowing *waqf* which limits the potential value of *mawquf* and therefore, its return. Plus, shares are also exposed to risk and founders might only endow risky shares. It might be the ill intention of founders to do that or (s)he simply do not have the knowledge to acquire profitable shares. This may cause *waqf* of shares to dissolve, hence, contradicting the perpetuity principle of *waqf*. Or, YWM may screen and assess the shares that the public choose to endow as *waqf*. Still, this process will add another layer of bureaucracy similar to land assessment for *waqf*.

Meanwhile, Academician E suggested cash, "we can *waqf* in form of cash". Academician G is also in support of this, "I think the one that is really convenient to finance the economy and to governments basically being expenditure or economics or budget or whatever for public finance is the cash *waqf*". Academician G asserted further that BNM has a tendency to regulate high value of cash due to its liquidity:

> We talk to the regulators, we have a hostel, we have example of property, this and that, we have property to run, we have a campus to run, we have shopping mall, I don't think the Central Bank will be interested to come and talk to you. But if you tell him we have one billion endowments cash *waqf*, well that's a concern to me. Because I'm concern about liquidity. So, why not you regulate that money or *waqf* which is based on cash.

Liquidity in this case, is how easy it is for cash to be invested in the Islamic capital market or formed into a financial instrument. It is also interesting to note that Academician G's concept of cash *waqf* is similar to Mohsin (2013) i.e. dedicating the

usufruct and not the capital for the benefit of welfare. This is unlike the definition of JAWHAR (2010a) in which the capital itself is used for the benefit of welfare. Hence, cash *waqf* can actually be formed into a financing vehicle that can generate return, much like *waqf* of shares.

Cash *waqf* presents opportunity to the middle-income group that usually do not own land to endow *waqf* and reap heavenly rewards too. By logic, every individual possesses cash, hence, significantly increases the potential value of *mawquf*. This is further encouraged through tax exemption. Moreover, unlike *waqf* of shares, cash *waqf* in and of itself does not contain risk. True, its value may reduce due to the time value of money (the money today is worth more than the same amount of it in the future) but the manner and avenues of its investment can result in increased value. In addition, since YWM can hire a professional fund manager, there will be no need for assessment like shares that was mentioned earlier. Lastly, in comparison to *waqf* land, cash *waqf* has marginal issues. Therefore, cash is the most suitable *mawquf* for *waqf* financing expenditures.

6.2.3.2 Investment of Cash *Waqf* in Islamic Unit Trust Fund

Now that cash *waqf* has been decided, we should determine the most appropriate cash *waqf* investment mode that can optimise return without violating the *Shari'ah* requirements of *waqf* nor any other typical *Shari'ah* prohibition like usury. As is the opinion of Academician C and Academician G respectively:

There are many other methods that can be use such as *sukuk*, Islamic bond and such including *waqf* REITs and contracts like *waqf* shares, *waqf* of shares, corporate *waqf,* *waqf* movable, immovable, cash *waqf,* and others. So meaning, to develop *waqf* property, in order to provide more profits, better benefits to the *waqf* beneficiaries,

they have to explore this type of Islamic commercial transaction contract rather than using the orthodox one.

So meaning that we have to restructure, to rebrand, to reproduce the *waqf* in a different structure, in a different product, portfolio, and services that to the language of the regulators, Central Bank and Securities Commission and also convenient to the financial market.

Thus, new financing method should be considered in lieu of the traditional ones.

Academician E gave one specific suggestion:

Number three I think is about the vehicles, vehicles we talking about how we are going to develop the prospect, the *waqf* asset, what are the prospective investment, what will be the kind of vehicle. For example, now probably we [i.e. the public] have not many land or sort of fix asset to [endow as] *waqf* but we can [endow] *waqf* in form of cash. So how are we going to convert this cash to become like unit trust…

Academician G argued along the same line but with more vision:

Waqf especially the cash *waqf*, one of its unique features is that capital cannot be depleted, shrink, and reduced. So, if we are talking about one billion [Ringgit], one billion [Ringgit] will stay there. So, it creates a long lasting sustainable funds. So, one billion [Ringgit] is always there. Now, you just invest the one billion [Ringgit] and the one billion [Ringgit] you never touch it. So [you get] the proceed of the one billion [Ringgit]. So today at one billion [Ringgit] you will get at I don't know at many percent. Let's say you are taking return of 15%. So, 15% of the one billion [Ringgit]. Tomorrow, and the coming future, so the one billion [Ringgit] keeps expanding, growing.

Meshing the opinions of Academician G and Academician E, cash *waqf* should be invested in a portfolio of investment. The OIC Fiqh Academy in its Resolution No.140 (15/6) highly encourages diversification of investment in addition to investing in *Shari'ah*-compliant products. Hence, cash *waqf* investment in unit trust fund is the best fit. SC (2008) states the definition of unit trust fund as "a type of collective investment scheme that offers investors the opportunity to invest in a diversified portfolio of Shariah-compliant securities, sukuk, and money market instruments" (SC, 2014, p.42). As can be seen from the definition, unit trust fund invests in different *Shari'ah*-compliant company shares and other financial instruments which is diversification at play.

This idea of *waqf* unit trust fund is not alien and had been practiced before in Indonesia. The *waqf* unit trust fund consists of fixed income fund which are Islamic bond, repurchase agreement (REPO), and Islamic money market (Siswantoro & Dewi, 2011). It was initiated through a collaboration between Dompet Dhuafa (the trustee of *waqf*) and Batasa Capital (a financial service solution providing firm). However, due to lack of transparency, public awareness, and risk management, the Indonesian *waqf* unit trust fund was terminated in 2006 (Siswantoro & Dewi, 2011). Perhaps the reason for poor risk management was because the *waqf* unit trust fund had only focused on investing in fixed income assets without considering investment in stocks, a clear disregard of Portfolio Theory.

Nonetheless, investment always carry risk. Then again, risk is a universal issue in finance. As elaborated by Academician G:

> The other thing is there are some other risk but I think that one to me is normal. If you have a cash *waqf* structures as part of the let's say endowment of the government to support some of the economic sectors so possible depletions, possible loss of the cash, you may incur some losses, a little bit issue of inflations, what kind of investment

you want to invest, how much is the amount, who will run this one but I don't think these are unique issues for this *waqf* but this are common features, risk in any cash, in any liquidity, so it is applicable for cash investments, applicable for the cash *waqf*. So, I don't see it is unique to cash *waqf*. This is a very generic issue.

Based on the above discussion, *Shari'ah* scholars should deliberate on this fact; whether the inevitable loss in investment despite performing rigorous evaluation on risk management could be similar to natural disasters that destroy *waqf* properties. In the case of *waqf* for expenditure, this thesis suggests that the federal government should compensate the loss whenever the loss erodes the initial value of *mawquf*. This is because ultimately, it is the government's duty to care for its citizens. The recommendation is based on the statement made by Academician H who had stressed that *waqf* should play a complementary role instead of taking over the government's duty completely.

In forming the *waqf* unit trust fund, YWM should collaborate with an Islamic unit trust firm so that the portfolio of assets in the *waqf* unit trust fund is selected and monitored by a professional fund manager. This injects credibility in the *waqf* unit trust fund, ensures risk management, and follows the recommendation made by Industry Expert B on strategic collaboration. This public-private sector relationship is also inspired by the real collaboration of PWS and BMMB that was discussed in Section 2.4.3. It had inadvertently address the shortage of manpower and broad job scope that SIRCs faced. Islamic unit trust firm also has vast experience and knowledge in the governance of unit trust fund in comparison to YWM. It is the norm for annual and intermittent reports to be published by the firm which is much needed for *waqf* financing expenditures to gain the trust of the general public.

To guarantee that the *waqf* unit trust fund is *Shari'ah* compliant, it should go through a screening process:

I think you have to bring *Sha'riah* advisors on any endowment funds especially under the sectors in economics of the government to make sure the operations of the cash *waqf* is appropriate, is compliance under the *Shari'ah*, there must be some kind of troubleshooting, rectification and so on so forth, should be subjected to *Shari'ah* audit, should be subjected to *Sha'riah* review, and so on so forth. So, this kind of governance I think should be part of it.

The SC had demonstrated its willingness to regulate cash *waqf* investment in the Islamic capital market, including Islamic unit trust fund (SC, 2014). However, the SC must screen YWM as the trustee, and the Islamic unit trust firm as the fund's management company beforehand (SC, n.d.). The *waqf* unit trust fund must also be screened by the SC through its own *Shari'ah* Advisory Council (SAC) to make sure it is *Shari'ah* compliant. As a result, the structure of cash *waqf* investment is depicted in Figure 6.3.
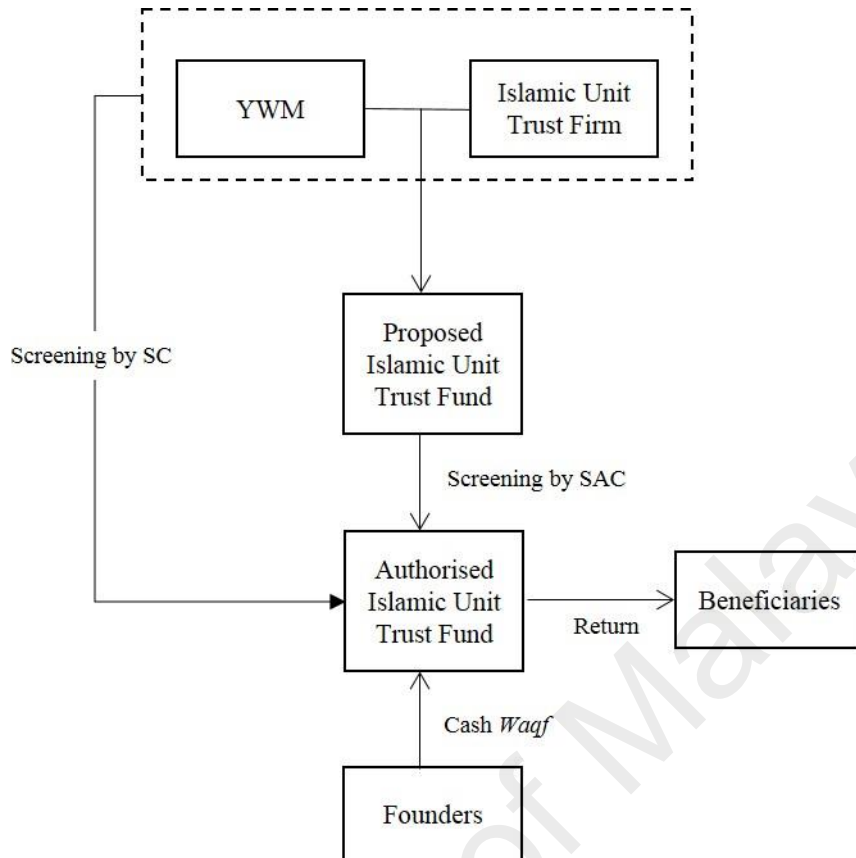
Figure 6.3: The Structure of Cash *Waqf* Investment

6.3   The Blueprint for Financing Public Expenditures through *Waqf*

So far, we have addressed disjointedly the issues on the comprising components for the model of *waqf* financing public expenditures. Results from interviewees' transcripts showed that cash is the most suitable type of *mawquf*, investment in an Islamic unit trust fund is appropriate, as well as YWM should be the trustee together with an Islamic unit trust firm. The founders are the general public and beneficiaries of the *waqf* are specific expenditure items. Deliberation of these inputs result in the *waqf* model depicted in Figure 6.4.
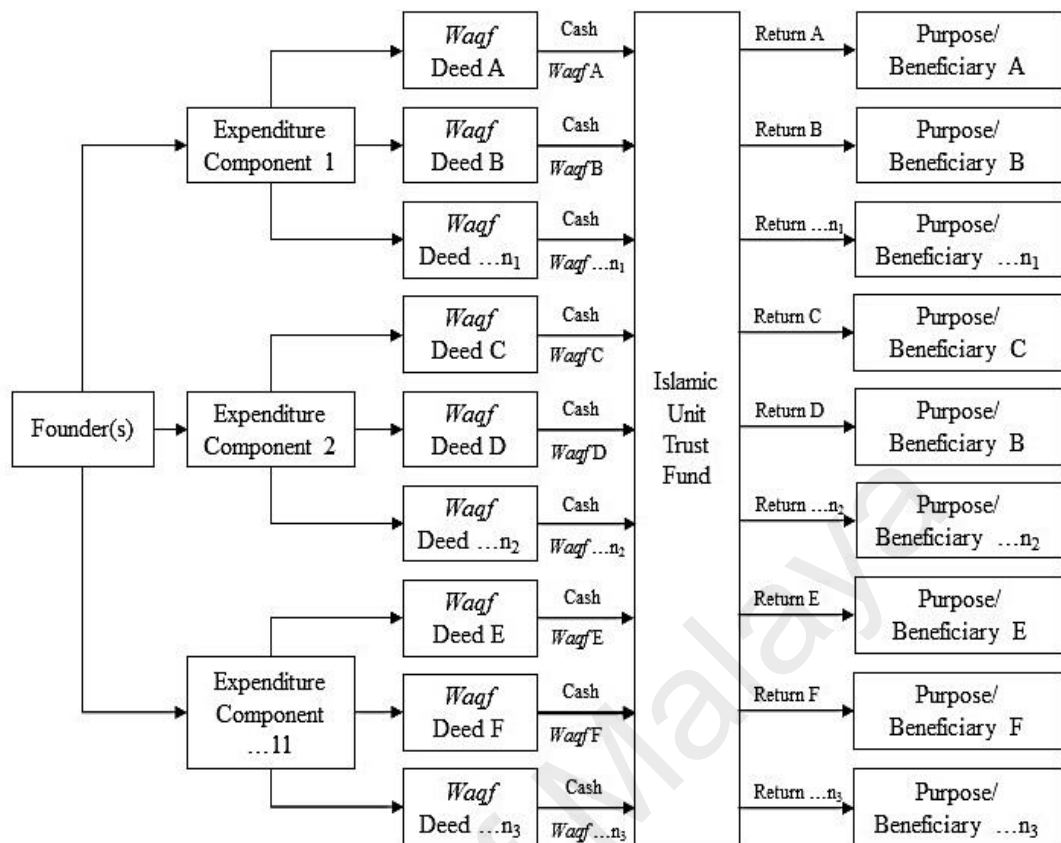
Figure 6.4: Model for *Waqf* Financing Public Expenditure

Waqif can select which federal government expenditure component(s) that (s)he wishes to endow at the YWM website. From there, (s)he can select the end beneficiary from the different *waqf* deeds offered by YWM. These *waqf* deeds are in forms so the *waqif* can then fill up the forms as was discussed in Section 6.2.2.2. Then the founders can transfer a voluntary sum of cash online to the Islamic unit trust fund plus management fee, thus, rendering the cash as *waqf*. YWM's system will register the total of cash collected from different founders corresponding to each *waqf* deed. Note that an online system such as this reduces bureaucracy significantly. Returns from the cash *waqf* corresponding to each *waqf* deed are then channelled to the rightful beneficiaries.

6.4   Tackling Other Issues

The remaining issues are court settlement, supply and distribution of public goods, as well as *waqf* lands. Since these are irrelevant to the comprising components of the *waqf* model, this thesis will only deliberate on these issues briefly while making full use of the results obtained from the interviewees' transcripts.

The issue of court settlement usually involves cases such as revocation of the *waqf* status or when founders feel unsatisfied towards the management of *waqf* trustee (YWM) and/or the *waqf* fund. Academician B was concerned because matters of *waqf* are usually adjudicate at *Shari'ah* court but the founders and beneficiaries of *waqf* for public expenditure also comprise of non-Muslims. Recall that Item 1 of the Ninth Schedule under List Two – State List of the Federal Constitution states that *Shari'ah* court only has jurisdiction on Muslims. It does not cover matters such as defence, economics, finance, and other components that relate to the federal government expenditure.

Marican (2013) had already dissected this issue by referring to Article 74(1), Item 8(c) in the Federal List, and Article 75 of the Federal Constitution. Since Article 75 has already been explained earlier in this thesis, only the first two are quoted respectively below:

Without prejudice to any power to make laws conferred on it by any other Article, Parliament may make laws with respect to any of the matters enumerated in the Federal List or the Concurrent List (that is to say, the First or Third List set out in the Ninth Schedule) (p.72).

Trade, commerce and industry, including – (c) incorporation, regulation and winding up of corporations other than municipal corporations (but including the municipal

180

corporation of the federal capital); regulation of foreign corporations; bounties on production in or export from the Federation (p.195).

By highlighting SIRC of Selangor as a corporate body and not a natural person that professes himself as a Muslim, Marican (2013) claimed that suits against SIRC of Selangor should be handled in civil court. Similar applies to YWM since it is a corporate body. Even if there is provision in the state law that stipulates otherwise, Marican (2013) clarified that Article 75 would cause the stipulation nullified. As with the case of non-Muslim involvement, settlement will also be carried out in civil court (Marican, 2013).

The second issue pertains to the supply and distribution of public goods raised by Industry Expert A. In terms of the former, Industry Expert A was referring to the situation when the Islamic unit trust fund has generated returns and gave it to Likas Hospital in Sabah, for example. Assuming that the hospital intends to purchase a number of health equipment and medications, to whom should the hospital get the supplies from? Since the hospital has long been in operation and has its own management, there is no wrong to simply let the hospital's management decide. As for the latter, Industry Expert A was referring to the choice of beneficiaries i.e. which sector, to which state, and for what purpose should YWM design the *waqf* deeds upon. This can be determined according to the federal government's budget announced every year at which YWM can specify those sectors that are experiencing budget cuts. Apart from that, YWM should also welcome suggestions from the Malaysian public. Distribution will then be decided on the *waqf* deeds that receive cash *waqf* and earn return.

As for the last issue, Industry Expert B gave an idea, "Create a specific Act for *waqf* lands in order to promote *waqf* development". The recommended *Waqf* Land Act should include among others, provision on *waqf* land registration, and process of converting

lands into *waqf*. The Act can certainly resolve the confusion of the different processes and laws adopted by different states regarding *waqf* lands.

6.5   Conclusion

Chapter 6 had proposed a model for *waqf* financing Malaysian public expenditures i.e. subsidies and all the Malaysian federal government expenditure excluding general administration. This thus fulfil RO 2 and RQ 3. The major founders of this *waqf* model are the general Malaysian public, while the beneficiaries are obviously the determined federal government expenditures. Other specific comprising components of the model on the other hand, were determined by addressing most of the issues identified in Chapter 5.

The first main issue was the question of trustee for *waqf* financing public expenditure and the differences in state laws. Examination of the interviewees' answers revealed that partial centralisation of *waqf* law is the best solution. SIRC remain as the trustee of religious *waqf* and private *waqf*, while YWM is the trustee for philanthropic *waqf*. Meaning, the trustee of *waqf* for public expenditure is YWM which is governed by the Federal Territories *Waqf* Act. YWM should be given the authority to give permission to other parties to manage their own *waqf* of public goods and declare other parties as *nazir khas*, just like Section 4(1)(a) and Section 4(1)(c) from *Wakaf* (State of Selangor) Enactment 2015. As such, state laws still have the freedom to stipulate its own *waqf* laws regarding religious and private *waqf*. Therefore, Rulers' sensitivities and development for *waqf* financing public expenditure are both mediated.

The second main issue is the management of *waqf* for public expenditure. It pertains to lack of transparency and human expertise which may destroy public trust. Thematic analysis suggests three solutions to the dilemma namely publication of *waqf* reports,

specification of *waqf* deed, and strategic collaboration with an Islamic unit trust firm. Reports on the *waqf* activities can educate the public about its applicability outside of pure religiosity motives, *waqf* deed specification may negate the notion of voluntary tax, while strategic collaboration will result in manageable investment risk. An indirect result of all this could be a rise in the contribution of *waqf* for public expenditure.

The third and last major issue concerns *mawquf* i.e the form of *mawquf* that is appropriate for public expenditure (philanthropic *waqf*) and its mode of investment. The latter is especially important because distributing returns instead of the capital of the *waqf* will ensure perpetuity. Interview results show that cash is the most appropriate *mawquf* due to tax exemption, liquidity, and the fact that everyone has it. Meanwhile, Islamic unit trust fund is the suitable mode of investment since it is *Shari'ah* compliant and employs diversification strategy which can help mitigate risk. Should there be losses to the extent that the original value of *mawquf* is minimised, then the federal government will compensate that loss value of *mawquf*.

In addition, these findings had helped determine the required data to complete the theoretical model outlined in Section 4.5.1. Specifically, the form of *mawquf* that is suitable for *waqf* financing public expenditure is cash, while the usufruct of *waqf* is return from an Islamic unit trust.

CHAPTER 7: QUANTITATIVE ANALYSIS: IMPACT OF WAQF FINANCING PUBLIC EXPENDITURE ON FEDERAL GOVERNMENT DEBT

7.1   Introduction

This chapter addresses the third and final objective of this thesis. To reiterate, RO 3 is "To analyse the impact that *waqf* has on Malaysian federal government debt in the event that *waqf* finances Malaysian federal government public expenditure". Meanwhile RQ 4, the RQ that corresponds to RO 3 is "How will *waqf* impact Malaysian federal government debt in the event that *waqf* finances Malaysian federal government public expenditure?"

The chapter is organised as follows. Section 7.2 presents the interviewees' opinion on the impact of *waqf* financing public expenditure on debt. Section 7.3 discusses on data sampling for input gathered from the qualitative findings of Chapter 6. Based on the similar input, a complete version of the theoretical model is presented in Section 7.4. From the theoretical model, the model equilibrium is derived in Section 7.5. Calculation for parameter values and steady state values are shown in Section 7.6 and 7.7 respectively. Shocks are introduced to initiate simulation and the results are presented in section 7.8. Finally, Section 7.9 concludes this chapter.

7.2   Impact of *Waqf* Financing Public Expenditure on Debt: The Interviewees' Perspective

Interviewees asserted that *waqf* financing public expenditure has an impact of decreasing federal government debt. Academician C, Government Official D, and Industry Expert A had stated this simply. Academician A also gave a similar opinion but had stressed that government should not be the trustee of *waqf*:

Well, *waqf* definitely can be made for instance to take over some areas or at least to support federal or local government such as street repairs, pavement repairs, maintenance… This *waqf* definitely indirectly help the federal government and the local government but again, they must not be in the hands of the government because eventually, government are less efficient and the likelihood of corruption in them is much higher than when it is run by private sector, private individuals, and strong supervision from the government. Indirectly, yes [government debt can be reduced].

Of course, it has been argued extensively in Chapter 6 that YWM is the suitable trustee for philanthropic *waqf,* after all. Hence, to not let government be the trustee of *waqf* is negligible. On the other hand, Academician B mentioned that federal government debt will reduce given that the issues identified were addressed, "Yes, I think so. For sure. If all those conditions are fulfilled". Chapter 5 had identified the issues while Chapter 6 had addressed them. Meanwhile, Academician D stated that *waqf* will be able to reduce debt but at a slow pace, "Can but for reducing debt the best institution is the use of *zakat* in which within one to two years all debt will be over". Zakat is not the topic of this thesis; hence, it will not be elaborated further.

Other interviewees also had the same opinion but they had argued with more rigour. From their arguments, two subthemes emerged corresponding to why *waqf* has an impact on reducing debt. The first subtheme is idle revenue. According to Academician E:

You can create endowment so the government can cut less on expenditure, on budget, on IPTS or institute of higher learning, on scholarship because they have form an endowment out of the *waqf* fund invested so when the government can cut this expenses the money can be used for other investment and also the money can be used for the government to pay out the debt.

Simply put, there is no need for government expenditure when institutions can generate their own revenue. Less government expenditure means more revenue and this can be channelled for debt payment. Industry Expert B deduced the same, "Yes because part of government budget allocation for expenditures in public projects can be diverted to pay off government debt". So did Government Official A, "As a consequence of that *waqf* application (i.e. *waqf* financing public expenditure), the government can use the remaining tax to pay down debt and others that are more important". These assertions have a basis in the literature whereby Mohd Umar et al. (2012) found that *waqf* can help government to save more and the savings can be used to finance debt.

In relation to this, Academician F made an excellent point:

Yes! But if they reduce the expenditure but they don't reduce the revenue, tax rate, people may not be willing to give *waqf* because I still have to pay tax like I used to pay last time isn't it? So, if you want people to give *waqf*, then you must also reduce the tax rate. When you reduce the tax rate, your expenditure rate also may go down. So, does it reduce the debt budget depends on how you balance. But I supposed theoretically possible. Possible!

Now cash *waqf* had been decided in Chapter 6 as the suitable form of *waqf* for financing public expenditure. Since it is already entitled for tax exemption under Section 44(6) of the 1967 Income Tax Act, data on federal government revenue had indirectly accounted for this.

The second subtheme is avoiding borrowing. As mentioned by Government Official B, "There is no need for the government to borrow. The government can use *waqf* to build projects such as schools and health centres thus reducing the dependence on borrowing". This is supported by Academician H:

Yes, if the projects tended towards development projects, I think yes, it can lessen government debt. Because government incur debt mainly for development expenditures. Development expenditures to provide infrastructure are actually expensive but the government must provide them. So government has to borrow. So I think yes. If *waqf* becomes strong, it can help reduce government debt [by not borrowing further].

Academician G was not only positive that debt can reduce but viewed *waqf* as a potential revenue for the federal government:

Oh yes, that's a 100%. Actually I was thinking one time to write a paper, to make a proposal, at least put structure, put framework, how *waqf* can basically not only reduce the government debt, to me that's a 100% yes, not only to reduce the deficit, in the budget, in the federal government debt, but basically to go beyond that and be contributing 50% on the government budget and expense in the future…

Academician G's vision is plausible because *mawquf* as a capital is perpetual in nature. The perpetual capital can be invested time and time again to accumulate returns until at one point in time, the returns can contribute to a value similar to 50% of the government budget. However, Academician G admitted that this can only happen in the far future.

Focusing back to the second subtheme, *waqf* financing public expenditures makes borrowing becomes unnecessary. In turn, deceleration of debt occurs. This findings coincide with Çizakça (1998). Notice also that these two subthemes argue from the fiscal standpoint which is revenue and borrowing. Hence, *waqf* financing public expenditure should be incorporated in the theoretical model through the behaviour of fiscal policy. As shown in Equation 4.5 in the theoretical model presented in Section 4.5.1, *waqf* return has already been modelled as such.

7.3   Further Data Sampling

Results from Chapter 6 showed that the form of *mawquf* that is suitable for *waqf* financing public expenditure is cash, while the usufruct of *waqf* is the return from an Islamic unit trust. However, this researcher was unable to obtain a consolidated data on cash *waqf*. Quarterly data was needed but some SIRCs can only provide yearly data, while others could not provide the data though it was requested repetitively. Therefore, not only that a normal data set cannot be obtained, a consolidated data with matching time period frequencies is also impossible. Indeed, bureaucracy and transparency are issues for *waqf* in Malaysia, which were discussed in Section 5.3.2.

Still, very scarce research had actually analysed the impact of *waqf* financing public expenditure on debt, even more so quantitatively. On top of that, not much attention is given to the third sector in the workings of modern economy. Hence, despite the lack of comprehensive cash *waqf* data, the study should still be carried out to address these large gaps and answer RO3. It is possible by analysing the effects of a change in Islamic unit trust return as oppose to a change in cash *waqf* contribution. This is also rational because the return may change and not the *mawquf* due to the perpetuity principle.

This thesis decides to use quarterly returns of Public Ittikal (P Ittikal) Fund from the third quarter of 1997 to the fourth quarter of 2015 as a proxy for Islamic unit trust fund. The said unit trust fund makes up of nearly 90 percent *Shari'ah* compliant equities and related securities from among others, Tenaga Nasional Berhad, Telekom Malaysia Berhad, Sime Darby Berhad, IHH Healthcare Berhad, and Axiata Group Berhad (Public Mutual Berhad [PMB], 2016). Thus, it matches with the argument of the place of public *waqf* in Malaysian economy (Figure 2.8) in that collected cash *waqf* are connected with firms through investments.

P Ittikal Fund is the earliest and one of many PMB *Shari'ah* based unit trust funds. Although returns from P Ittikal Fund and returns from firms appear different outwardly, the two are in essence similar. This is because P Ittikal comprises of mostly *Shari'ah* compliant equities and securities from different firms so the net asset value (NAV) of the fund is determined by the capital gains and dividends from those firms. Due to this fact, the returns from unit trust fund is a suitable proxy for returns by firms too.

7.4   The Complete Theoretical Model

Now that cash *waqf* has been determined as the suitable form of *mawquf* and investment in Islamic unit trust as a way to ensure perpetuity, a complete theoretical model is presented below. To minimise confusion, it must be inform that the aforementioned qualitative findings cause most of the equations in Section 4.5.1 to change.

7.4.1   Households

The economy consists of many households where each make economic decisions. In order to analyse only one economic decision, the concept of a representative household agent is employed. We assume further that all agents have similar preference. Two functions to be defined for household is the utility function and budget constraint.

Households decide on total consumption, C_t^τ, and leisure, O_t, that are subjected to a budget constraint in order to attain utility or happiness. Total consumption is the amount of goods and services consumed by the representative agent while leisure is the remaining time left after labour services (L_t). Due to the altruistic behaviour of the representative agent, cash *waqf* contribution essentially becomes part of his consumption. Hence, C_t^τ can be broken down into consumption (C_t) and cash *waqf* contribution (V_t):

$$C_t^\tau = C_t + V_t \tag{1.2}$$

It is also important to state that total available discretionary time is normalised to 1 and leisure is the total available discretionary time minus labour services or working time. This means that equation containing O_t and L_t can be written as follows:

$$O_t + L_t = 1$$

$$O_t = 1 - L_t \tag{1.3}$$

As was mentioned, the utility of the representative agent is constraint by a budget. The representative household is the owner of productive factors namely capital, K_t and labour, L_t. By renting these productive factors to firms, the representative agent receives R$_t$ which is the return for K_t and wage, W_t as return for his L_t. V_t also counts as a productive factor but as per *waqf* deed, return from V_t is not gained by the household agent but is used for chosen federal government public expenditure. After paying for tax, T_t, earnings from the household agent is spent on C_t and V_t while the remaining is put into savings, S_t. We assume further that due to a competitive sector, S_t is directly transform into investment, I_t, and federal government bonds, B_t, without any cost thus:

$$S_t = B_t + I_t \tag{1.4}$$

The agent receives a return of R_t^r from purchasing past bonds B_t while I_t follows a process of capital accumulation overtime following a simple inventory accumulation equation:

$$I_t = K_{t+1} - (1 - \delta)K_t \tag{1.5}$$

Although Equation 1.5 is theoretically correct, capital is actually decided yesterday making capital a predetermined variable. This transforms Equation 1.5 into Equation 1.6:

$$I_t = K_t - (1 - \delta)K_{t-1} \tag{1.6}$$

Therefore, the intertemporal maximisation problem of the representative household agent is given as:

$$\max E_t \sum_{t=0}^{\infty} \beta^t U[C_t, O_t, V_t] \tag{1.7}$$

such that

$$C_t + V_t + S_t = W_t L_t + R_t K_{t-1} + B_{t-1}(1 + R_t^r) - T_t \tag{1.8}$$

Equation 1.7 is the utility function of the representative household while β, $\beta \in (0,1)$ is the intertemporal discount factor which specifies how much the agent values his/her future utility as oppose to his/her current utility. Equation 1.8 is the household's budget constraint.

To facilitate simple calculation, the utility function can be expressed in a log linear form. Further substituting Equation 1.3 into Equation 1.7 as well as Equation 1.4 and Equation 1.6 into Equation 1.8:

$$\max \ E_t \sum_{t=0}^{\infty} \beta^t [\mu \log C_t + \gamma \log(1 - L_t) + \eta \log V_t] \tag{1.9}$$

such that,

$$C_t + V_t + K_t - (1 - \delta)K_{t-1} + B_t = W_t L_t + R_t K_{t-1} + B_{t-1}(1 + R_t^r) - T_t \tag{2.0}$$

μ, γ, and ν are the preference parameter for C_t, $1 - L_t$, and V_t respectively where $\mu + \gamma + \eta \approx 1$. Specifically, μ represents the proportion of consumer spending to total income, γ represents the proportion of leisure to total income, and η represents the proportion of cash *waqf* endowment to total income. In economic terms, μ can also be defined as the marginal propensity to consume, γ as the marginal propensity to leisure,

and η as the marginal propensity to endow cash *waqf*. Basically, these preference parameters indicate the agent's preferences toward consumption – leisure – cash *waqf* endowment decisions.

Household will want to maximise C_t, V_t, L_t, K_t, and B_t. This household problem can be solved using a dynamic Lagrangian calculation before deriving first order conditions (FOCs):

$$\mathcal{L} = \sum_{t=0}^{\infty} \beta^t \begin{bmatrix} \mu \, log \, C_t + \gamma log(1 - L_t) + \eta \, log \, V_t \\ \\ \\ - \lambda_t [C_t + V_t + K_t - (1 - \delta)K_{t-1} + B_t - W_t L_t - R_t K_{t-1} - B_{t-1}(1 + R_t^r) + T_t] \end{bmatrix}$$

λ_t is the Lagrange multiplier of period t. As the capital for a given period appears in time t-1 and in time t, the restriction faced by households at time t is:

$$... - \beta^t \lambda_t [C_t + V_t + K_t - (1 - \delta)K_{t-1} + B_t - W_t L_t - R_t K_{t-1} - B_{t-1}(1 +$$

$$R_t^r) + T_t] - \beta^{t+1} \lambda_{t+1} [C_{t+1} + V_{t+1} + K_{t+1} - (1 - \delta)K_t + B_{t+1} - W_{t+1}L_{t+1} - R_{t+1}K_t -$$

$$B_t(1 + R_{t+1}^r) + T_{t+1}] \tag{2.1}$$

The first order conditions (FOCs) of the household problem are:

$$\frac{\partial \mathcal{L}}{\partial C} = \beta^t \left[\frac{\mu}{C_t} - \lambda_t \right] = 0$$

$$\lambda_t = \frac{\mu}{C_t} \tag{2.2}$$

$$\frac{\partial \mathcal{L}}{\partial L} = \beta^t \left[\frac{\gamma}{1 - L_t}(-1) + \lambda_t W_t \right] = 0$$

$$\lambda_t W_t = \frac{\gamma}{1 - L_t} \tag{2.3}$$

$$\frac{\partial \mathcal{L}}{\partial V} = \beta^t \left[\frac{\eta}{V_t} - \lambda_t \right] = 0$$

$$\lambda_t = \frac{\eta}{V_t} \tag{2.4}$$

$$\frac{\partial \mathcal{L}}{\partial K} = -\beta^t \lambda_t + \beta^{t+1} \lambda_{t+1} [R_{t+1} + 1 - \delta] = 0$$

$$\beta^t \lambda_t = \beta^{t+1} \lambda_{t+1} [R_{t+1} + 1 - \delta]$$

$$\frac{\lambda_t}{\lambda_{t+1}} = \beta [R_{t+1} + 1 - \delta] \tag{2.5}$$

$$\frac{\partial \mathcal{L}}{\partial B} = -\beta^t \lambda_t + \beta^{t+1} \lambda_{t+1} [1 + R_{t+1}^r] = 0$$

$$\beta^t \lambda_t = \beta^{t+1} \lambda_{t+1} [1 + R_{t+1}^r]$$

$$\frac{\lambda_t}{\lambda_{t+1}} = \beta [1 + R_{t+1}^r] \tag{2.6}$$

By equating Equations 2.2 and 2.4, we obtain:

$$V_t = \frac{\eta}{\mu} C_t \tag{2.7}$$

Equation 2.7 determines the agent's decision between endowing cash *waqf* or consuming. Basically, the right hand side of Equation 2.7 is the opportunity cost of endowing an additional unit of cash *waqf*. Substituting Equations 2.2 into Equation 2.3, we obtain:

$$W_t = \frac{\gamma C_t}{\mu (1 - L_t)} \tag{2.8}$$

Equation 2.8 equates the marginal rate of substitution between consumption and leisure $\left(\frac{\gamma}{\mu} \right)$ to the opportunity cost of an additional unit of leisure (W_t). Another way to view W_t is to substitute Equation 2.4 into Equation 2.3 instead:

$$W_t = \frac{\gamma V_t}{\eta(1 - L_t)} \qquad (2.9)$$

Equation 2.9 equates the marginal rate of substitution between endowing cash *waqf* and leisure to the opportunity cost of an additional unit of leisure.

From Equation 2.2 we get:

$$\lambda_{t+1} = \frac{\mu}{C_{t+1}} \qquad (3.0)$$

Substituting Equation 3.0 and Equation 2.2 into Equation 2.5 and Equation 2.6:

$$\frac{C_{t+1}}{C_t} = \beta[R_{t+1} + 1 - \delta] \qquad (3.1)$$

$$\frac{C_{t+1}}{C_t} = \beta[1 + R^r_{t+1}] \qquad (3.2)$$

Equation 3.1 defines the condition of the agent's decision about investment. Basically, the agent compares the utility of consumption with that of investment. On the other hand, Equation 3.2 indicates that the agent compares the utility of consumption with that of purchasing bonds.

7.4.2   Firms

Firms rent L_t and K_t from households. These production factors are then converted into final goods (Y_t). Firms then pay labour $W_t L_t$ and $R_t K_{t-1}$ to households while channelling return $V_t D_t$ to the federal government. D_t is simply the rate of return for cash *waqf*. The federal government is obliged to use $V_t D_t$ to finance for identified public expenditures only. Since the sole owners of production factors are the households, firms do not make investment decision nor decide on the amount of hired inputs from period to period. This is to simplify the theoretical model following Torres (2013). It causes the

maximisation problem of the firm to become a static equation and changes from Equation 3.3 (from Section 4.5.1.2) to Equation 4.9:

$$\pi = Y_t - W_t L_t - R_t K_{t-1} - V_t D_t \qquad (4.9)$$

Changes in the firm's maximisation problem thus changes all the other behavioural equations of the firm. Y_t also follows a Cobb-Douglas production function and has constant returns to scale whereby V_t is included as the production factor:

$$Y_t = A_t F(K_{t-1}, L_t, V_t) = A_t K_{t-1}^{\alpha} L_t^{\rho} V_t^{1-\alpha-\rho}$$

A_t is the technology or total factor productivity. Following Gali et al. (2007), we normalise A_t to unity and Y_t becomes:

$$Y_t = K_{t-1}^{\alpha} L_t^{\rho} V_t^{1-\alpha-\rho} \qquad (5.0)$$

α is the output elasticity of K_{t-1} and ρ is the output elasticity of L_t. Thus, the firm's maximisation problem becomes:

$$\pi = K_{t-1}^{\alpha} L_t^{\rho} V_t^{1-\alpha-\rho} - W_t L_t - R_t K_{t-1} - V_t D_t \qquad (5.1)$$

The firm maximises profit by choosing labour, capital, and cash *waqf* contribution. To solve the firm's problem, we take FOCs:

$$\frac{\partial \pi}{\partial L} = \rho K_{t-1}^{\alpha} L_t^{\rho-1} V_t^{1-\alpha-\rho} - W_t = 0$$

$$W_t = \rho K_{t-1}^{\alpha} L_t^{\rho-1} V_t^{1-\alpha-\rho} \qquad (5.2)$$

$$\frac{\partial \pi}{\partial K} = \alpha K_{t-1}^{\alpha-1} L_t^{\rho} V_t^{1-\alpha-\rho} - R_t = 0$$

$$R_t = \alpha K_{t-1}^{\alpha-1} L_t^{\rho} V_t^{1-\alpha-\rho} \qquad (5.3)$$

$$\frac{\partial \pi}{\partial V_t} = (1 - \alpha - \rho)K_{t-1}^{\alpha}L_t^{\rho}V_t^{-\alpha-\rho} - D_t = 0$$

$$D_t = (1 - \alpha - \rho)K_{t-1}^{\alpha}L_t^{\rho}V_t^{-\alpha-\rho} \tag{5.4}$$

Substituting Equations 5.0 into Equation 5.2, 5.3, and 5.4 we respectively obtain:

$$W_t = \frac{\rho Y_t}{L_t} \tag{5.5}$$

$$R_t = \frac{\alpha Y_t}{K_{t-1}} \tag{5.6}$$

$$D_t = \frac{(1 - \alpha - \rho)Y_t}{V_t} \tag{5.7}$$

Equations 5.5 to 5.7 show that the rate of productive factors (wage, capital return, and cash *waqf* return) are a constant proportion of the total output over factor quantity ratio.

7.4.3 Federal government

The federal government budget constraint is given as:

$$B_t = B_{t-1}(1 + R_t^r) + G_t - T_t - V_t D_t \tag{4.0}$$

The government borrows B_t when T_t and value of return from cash *waqf*, $V_t D_t$ are insufficient to finance for total federal government expenditures, G_t (i.e. sum of federal government operating and development expenditure), federal government debt B_{t-1}, and interest on that debt (R_t^r). Hence Equation (4.0) states that bond financing is employed to finance expenditure, service debt, and when usufruct from *waqf* is insufficient to finance the selected public expenditures. It must be stressed that the federal government's responsibility as a *mutawalli* is to spend the return of cash *waqf* on specified public expenditures only.

Let $\hat{S}_t = T_t - G_t$ and dividing Equation 4.0 by Y_t:

$$b_t = b_{t-1}(1 + R_t^r) - \hat{s}_t - v_t D_t \qquad (4.1)$$

whereby,

$$b_t = \frac{B_t}{Y_t} \qquad (4.2)$$

$$v_t = \frac{V_t}{Y_t} \qquad (4.3)$$

$$\hat{s}_t = \frac{\hat{S}_t}{Y_t} \qquad (4.4)$$

The fiscal policy rule that determines the primary balance-to-GDP ratio, $\hat{s}_t$ is specified as:

$$\hat{s}_t = \theta_0 \bar{\bar{s}} + \theta_1 \hat{s}_{t-1} + \theta_2 D_t + e_1 \qquad (4.5)$$

whereby, $\theta_0 = 1 - \theta_1 - \theta_2$. This manner of specification mimics Sakuragawa and Hosono (2011) and Torres (2013). Equation 4.5 simply states that the current primary balance-to-GDP ratio is determined by its steady state value ($\bar{\bar{s}}$), its past value, and the current rate of return from cash *waqf*, D_t. The insertion of D_t in Equation 4.3 captures the excess income from cash *waqf*.

7.4.4 Market Clearing

The feasibility constraint in the economy can be stated as:

$$Y_t = C_t + V_t + I_t + G_t \qquad (4.6)$$

whereby,

$$G_t = g_t Y_t \tag{4.7}$$

g_t is simply G_t over Y_t or the total federal government expenditure over GDP. It follows a AR(1) process:

$$g_t = (1 - \varphi)\bar{g} + \varphi g_{t-1} + e_2 \tag{4.8}$$

whereby, $\bar{g}$ is the steady state value of g. This form of specification follows Torres (2013).

Figure 7.1 shows the relationship between primary balance and debt. When primary deficit occurs (G-T), the value of debt increases. When primary surplus occurs (T-G), the value of debt decreases. Thus the incorporation of D in the primary balance (Equation 4.6) causes primary deficit to reduce which will eventually lead to primary surplus.
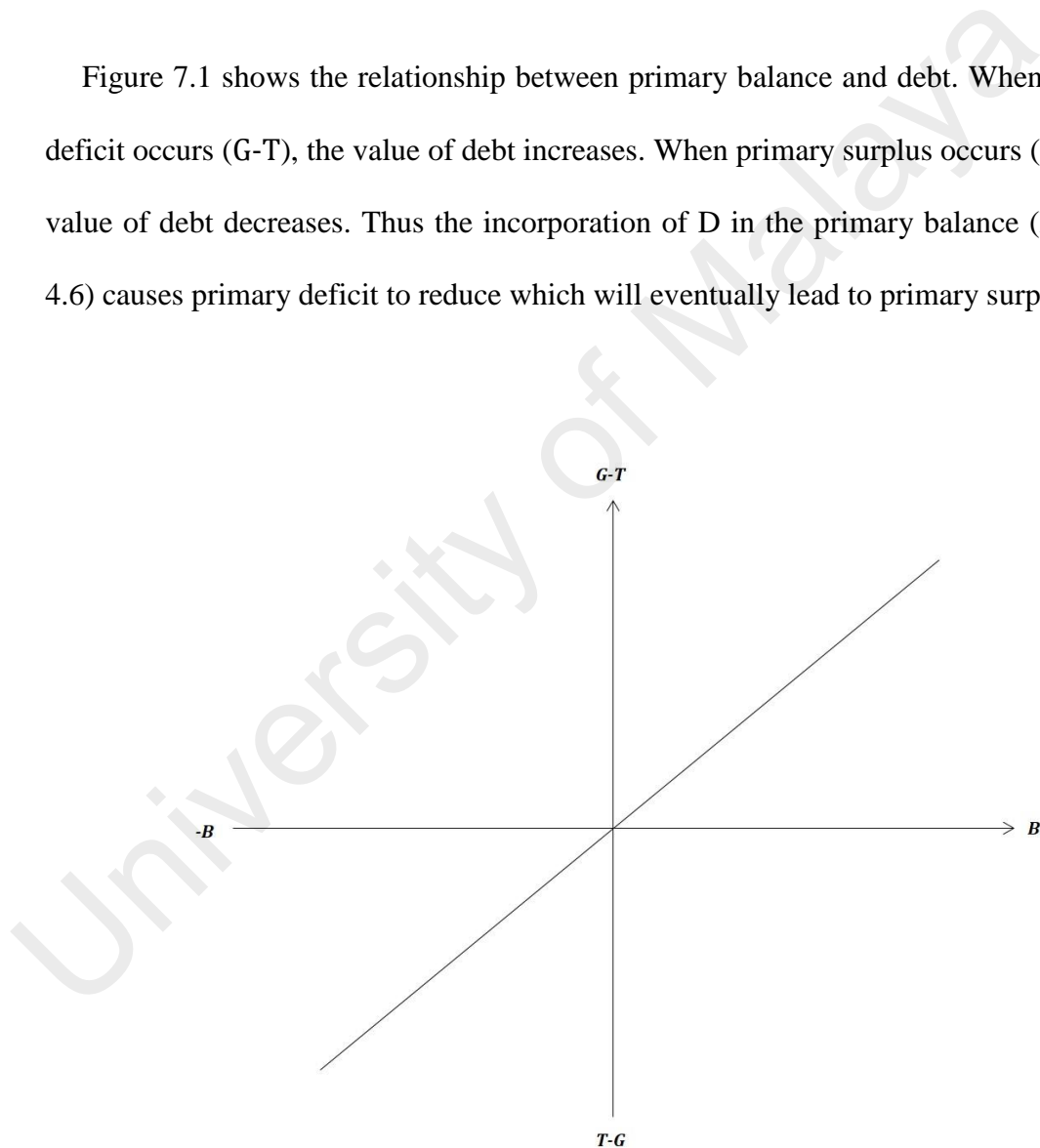
Figure 7.1: Relationship between Primary Balance and Debt

7.5   Model Equilibrium

The model equilibrium is derived from the theoretical model. It involves calculating sequences of endogenous variables which are C_t, L_t, V_t, K_t, W_t, R_t, I_t, R_t^r, D_t, G_t, Y_t b_t, v_t, $\hat{s}_t$, and g_t such that the balance path conditions are satisfied. Since there are 15 endogenous variables, thus 15 equations are needed to calculate the equilibrium of this modelled economy. These sets of equations are:

$$I_t = K_t - (1 - \delta)K_{t-1} \tag{1.5}$$

$$V_t = \frac{\eta}{\mu}C_t \tag{2.7}$$

$$W_t = \frac{\gamma C_t}{\mu(1 - L_t)} \tag{2.8}$$

$$\frac{C_{t+1}}{C_t} = \beta[R_{t+1} + 1 - \delta] \tag{3.1}$$

$$\frac{C_{t+1}}{C_t} = \beta[1 + R_{t+1}^r] \tag{3.2}$$

$$Y_t = K_{t-1}^{\alpha} L_t^{\rho} V_t^{1-\alpha-\rho} \tag{5.0}$$

$$W_t = \frac{\rho Y_t}{L_t} \tag{5.5}$$

$$R_t = \frac{\alpha Y_t}{K_{t-1}} \tag{5.6}$$

$$D_t = \frac{(1 - \alpha - \rho)Y_t}{V_t} \tag{5.7}$$

$$b_t = b_{t-1}(1 + R_t^r) - \hat{s}_t - v_t D_t \tag{4.1}$$

$$v_t = \frac{V_t}{Y_t} \tag{4.3}$$

$$\hat{s}_t = \theta_0 \bar{\hat{s}} + \theta_1 \hat{s}_{t-1} + \theta_2 D_t + e_1 \tag{4.5}$$

$$Y_t = C_t + V_t + I_t + G_t \tag{4.6}$$

$$G_t = g_t Y_t \tag{4.7}$$

$$g_t = (1 - \varphi)\bar{g} + \varphi g_{t-1} + e_2 \tag{4.8}$$

7.6   Determining Parameter Values

Parameter values are acquired through extrapolation, OLS estimation, and values supplied by the literature. These methods are approved by Torres (2013) and are time efficient for a thesis that employs exploratory sequential design. Table 7.1 lists the parameter values.

The value of η is rather difficult to obtain because almost no recent studies has been done to determine its value for Malaysia. Hence this thesis uses the household consumption expenditure for year 2014, the latest report published by DOSM (2015). Unfortunately, there is no value recorded in the report for η. However, assuming that public awareness on *waqf* is heightened, the component of miscellaneous goods and services may as well be replaced with cash *waqf* endowment. Making that item as a proxy for η, η can thus be assigned its value of 0.074. Meanwhile, recreation services and culture is a proxy for γ which holds the value of 0.049. As a result, $\mu = 1 - 0.074 - 0.049 = 0.877$. A larger value of γ as oppose to η highlights the key difference (altruism) between this model with most of the models in the literature.

Meanwhile, Iwata, Khan, and Murao (2003) estimated using non parametric technique that α is 0.19 and ρ is 0.58 for Malaysia. The value of $\delta = 0.07$ is appropriate for Malaysia as claimed by Nagaraj (2005). $\beta = 0.97$ is deemed appropriate and taken from

Torres (2013). Using Eviews, $\theta_0, \theta_1, \theta_2$, and φ are estimated via OLS method as shown below.

Table 7.1: OLS Estimation of ŝ

```
Dependent Variable: S  CAP
Method: Least Squares
Date: 08/12/17  Time: 15:49
Sample (adjusted): 2000Q2 2015Q4
Included observations: 63 after adjustments
```

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.050408	0.008872	-5.681504	0.0000
S CAP(-1)	-0.057884	0.126924	-0.456054	0.6500
D_RETURN	-0.038708	0.055671	-0.695296	0.4896
R-squared	0.011674	Mean dependent var		-0.048928
Adjusted R-squared	-0.021270	S.D. dependent var		0.048332
S.E. of regression	0.048843	Akaike info criterion		-3.153969
Sum squared resid	0.143138	Schwarz criterion		-3.051915
Log likelihood	102.3500	F-statistic		0.354358
Durbin-Watson stat	2.055802	Prob(F-statistic)		0.703082

Note that symbols cannot be specified as a variable in OLS estimation using Eviews while certain alphabets are illegal. Hence in Figure 7.2, S CAP is actually $\hat{s}$ while D_RETURN is simply D. Hence Equation 4.5 can be specified as:

$$\hat{s}_t = -0.05048 - 0.057884\hat{s}_{t-1} - 0.038708D_t \qquad (5.8)$$

From Equation 5.8, the parameter values can be determined as:

$$\theta_2 = -0.038708,$$

$$\theta_1 = -0.057884$$

$$\theta_0 = 1 - (-0.038708) - (0.057884) = 1.096592$$

201

Table 7.2: OLS Estimation of g

Dependent Variable: G
Method: Least Squares
Date: 08/13/17   Time: 04:22
Sample (adjusted): 2000Q2 2015Q4
Included observations: 63 after adjustments

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.310667	0.033110	9.382851	0.0000
G(-1)	-0.176555	0.122003	-1.447131	0.1530

R-squared	0.033191	Mean dependent var	0.264330
Adjusted R-squared	0.017342	S.D. dependent var	0.067455
S.E. of regression	0.066867	Akaike info criterion	-2.540983
Sum squared resid	0.272745	Schwarz criterion	-2.472947
Log likelihood	82.04096	F-statistic	2.094189
Durbin-Watson stat	2.087469	Prob(F-statistic)	0.152980

Note also that results generated by Eviews always show variables as capital letters. Hence G(-1) in Figure 7.3 should actually be $g(-1)$. Hence Equation 4.8 can be specified as:

$$g_t = 0.310667 - 0.176555g_{t-1} \tag{5.9}$$

From Equation 5.1, the parameter value can be determined as:

$$\varphi = -0.176555$$

Table 7.3 lists all the parameter values. To ensure that the results are robust, the parameter values obtained through calibration and OLS are assumed to be baseline values. Meaning, a deviation of 1% or 0.01 from the parameter values are also subjected to simulation.

Parameter	Definition	Baseline Values	+0.01 Values	-0.01 Values
μ	Preference parameter of consumption	0.877	0.887	0.867
γ	Preference parameter of leisure	0.049	0.059	0.039
η	Preference parameter of *waqf* contribution	0.074	0.084	0.064
ρ	Output elasticity of labour	0.58	0.59	0.57
α	Output elasticity of capital	0.19	0.20	0.18
δ	Depreciation rate of capital	0.07	0.08	0.06
β	Intertemporal discount factor	0.97	0.98	0.96
θ_0	Parameter of fiscal policy rule	1.096592	1.106592	1.086592
θ_1	Parameter of fiscal policy rule	-0.057884	-0.047884	-0.067884
θ_2	Parameter of fiscal policy rule	-0.038708	-0.028708	-0.048708
φ	Parameter of expenditure per GDP	-0.176555	-0.166555	-0.186555

7.7 Steady State Values

The steady state values refer to the growth rate of endogenous variables that remain constant throughout time i.e. when the modelled economy has stationarised and is in equilibrium condition (Torres, 2013). This particular study decides to find the steady state values by using the method adopted in Torres (2013) which are solving simultaneously most of the equations in the model equilibrium while subjecting the remaining equations to OLS estimation. Following Torres (2013), the latter requires eliminating the equations' time subscript and solving simultaneously most of the equations in the model equilibrium. Thus the equations are converted into:

$$\bar{I} = \delta \bar{K} \tag{6.0}$$

$$\bar{V} = \frac{\eta}{\mu} \bar{C} \tag{6.1}$$

$$\bar{W} = \frac{\gamma \bar{C}}{\mu(1 - \bar{L})} \tag{6.2}$$

$$1 = \beta(\bar{R} + 1 - \delta) \tag{6.3}$$

$$1 = \beta(1 + \overline{R^r}) \tag{6.4}$$

$$\bar{Y} = \bar{K}^\alpha \bar{L}^\rho \bar{V}^{1-\alpha-\rho} \tag{6.5}$$

$$\bar{W} = \frac{\rho \bar{Y}}{\bar{L}} \tag{6.6}$$

$$\bar{R} = \frac{\alpha \bar{Y}}{\bar{K}} \tag{6.7}$$

$$\bar{D} = \frac{(1 - \alpha - \rho)\bar{Y}}{\bar{V}} \tag{6.8}$$

$$\bar{b} = \frac{\bar{\bar{s}} + \bar{v}\bar{D}}{\overline{R^r}} \tag{6.9}$$

$$\bar{v} = \frac{\bar{V}}{\bar{Y}} \tag{7.0}$$

$$\bar{Y} = \bar{C} + \bar{V} + \bar{I} + \bar{G} \tag{7.1}$$

$$\bar{G} = \bar{g}\bar{Y} \tag{7.2}$$

Note that the " ‾ " sign on the variables denote steady state variables.

Substituting $\delta = 0.07$ into Equation 6.0 and $\beta = 0.97$ into Equation 6.3 as well as Equation 6.4, we respectively obtain:

$$\bar{I} = 0.07\bar{K} \tag{7.3}$$

$$\bar{R} = 0.1009$$

$$\overline{R^r} = 0.03093$$

Inserting the values of $\alpha = 0.19$ and $\bar{R} = 0.1009$ into Equation 6.7, we get:

$$\bar{K} = \frac{\bar{Y}}{0.5311} \tag{7.4}$$

Replacing Equation 7.4 into Equation 7.3:

$$\bar{I} = 0.1318\bar{Y} \tag{7.5}$$

Substituting $\eta = 0.074$ and $\mu = 0.877$ into Equation 6.1, we get:

$$\bar{V} = 0.08438\bar{C} \tag{7.6}$$

From Equation 5.9, the steady state value of $\bar{g}$ can be derived:

$$(1 - \varphi)\bar{g} = 0.310667$$

$$\left(1 - (-0.176555)\right)\bar{g} = 0.310667$$

$$\bar{g} = 0.2640$$

Hence Equation 7.2 becomes:

$$\bar{G} = 0.2640\bar{Y} \tag{7.7}$$

Inserting Equations 7.5, 7.6, and 7.7 into Equation 7.1:

$$\bar{C} = 0.5572\bar{Y} \tag{7.8}$$

Inserting the values of $\gamma = 0.049$ and $\mu = 0.877$ into Equation 6.2:

$$\bar{W} = \frac{0.05587\bar{C}}{(1 - \bar{L})} \tag{7.9}$$

Substituting Equation 7.8 into Equation 7.9 and rearranging:

$$\overline{W}(1 - \overline{L}) = 0.03113\overline{Y} \qquad (8.0)$$

Substituting $\rho = 0.58$ into Equation 6.6 we obtain:

$$\overline{W} = \frac{0.58\overline{Y}}{\overline{L}} \qquad (8.1)$$

Substituting Equation 8.1 in Equation 8.0 we get $\overline{L} = 0.9491$. Substituting $\alpha = 0.19$ and $\rho = 0.58$ into Equation 6.5:

$$\overline{Y} = \overline{K}^{0.19}\overline{L}^{0.58}\overline{V}^{0.23} \qquad (8.2)$$

Assigning $\overline{L} = 0.9491$, Equation 7.4, Equation 7.6, and Equation 7.8 into Equation 8.2 we obtain $\overline{Y} = 0.3474$. Assigning $\overline{Y} = 0.3474$ and $\overline{L} = 0.9491$ into Equation 8.1 we obtain $\overline{W} = 0.2123$. Inserting $\overline{Y} = 0.3474$ into Equation 7.8 we obtain $\overline{C} = 0.1936$. Inserting $\overline{C} = 0.1936$ into Equation 7.6 we obtain $\overline{V} = 0.01634$. Substituting $\overline{V} = 0.01634$ and $\overline{Y} = 0.3474$ in Equation 6.8 we generate $\overline{D} = 4.89$. Substituting $\overline{V} = 0.01634$ and $\overline{Y} = 0.3474$ in Equation 7.0 we obtain $\bar{v} = 0.04704$. Substituting $\bar{v} = 0.04704$ and $\overline{D} = 4.89$ in Equation 6.9 we obtain:

$$\bar{b} = \frac{\bar{\bar{s}} + 0.03140(4.89)}{0.03093} \qquad (7.5)$$

Value of $\bar{\bar{s}}$ can be derived from Equation 5.8:

$$\theta_0\bar{\bar{s}} = -0.05048$$

$$1.096592\bar{\bar{s}} = -0.05048$$

$$\bar{\bar{s}} = -0.04603$$

Hence, using $\bar{\bar{s}} = -0.04603$, we get $\bar{b} = 5.9488$. Assigning $\bar{Y} = 0.3474$ to Equation 7.4, we get $\bar{K} = 1.6502$. Assigning $\bar{K} = 1.9366$ into Equation 7.3 we get $\bar{I} = 0.1155$. Finally, assigning $\bar{Y} = 0.3474$ to Equation 7.7 we get $\bar{G} = 0.09171$. Table 7.4 lists the steady state values of the modelled economy. The steady state values are assumed to be correct since Dynare did not issue a warning when the simulation was done.

Table 7.4: Steady State Values

Steady State	Values
$\bar{L}$	0.9491
$\bar{Y}$	0.3474
$\bar{W}$	0.2123
$\bar{R}$	0.1009
$\bar{C}$	0.1936
$\bar{V}$	0.01634
$\bar{I}$	0.1155
$\bar{K}$	1.6502
$\bar{v}$	0.04704
$\overline{R^r}$	0.03093
$\bar{D}$	4.89
$\bar{\bar{s}}$	-0.04603
$\bar{b}$	5.9488
$\bar{G}$	0.09171
$\bar{g}$	0.2640

7.8 Simulation Results

In this section, the procedure for simulation is explained and results from the simulation is presented. As has been mentioned earlier, this research has decided to use different levels of parameter values as in Table 7.3. In addition, various degree of shocks namely 1%, 5%, and 10% are further assign. The coding written in Matlab for 1% shock of e_1 and e_2 at baseline parameter values are presented in Appendix A and Appendix B respectively while the computations are presented in Appendix C and Appendix D respectively.

The first step in simulation is to induce shock to the model equilibrium. Shock is perturbation introduced to the system in order to observe the deviations of the variables in comparison to their steady state values and the trend of variables before the variables return to the steady state (Torres, 2013). For the purpose of this study, shock in ŝ and g are introduced to indicate an increase in *waqf* return and government expenditure respectively. As a consequence of this, IRFs of variables that are affected by the shock will be generated. The generated IRF of *b* will answer RQ4 corresponding to RO3. Non-generation of IRF of *b* also answers RQ4 and RO3 in which case, *waqf* financing public expenditure does not have any impact on debt.

7.8.1   Shock to Primary Balance to GDP

The shock on primary balance to GDP (Equation 4.5) indicates an increase in *waqf* return. Specifically, e_1 is increased to 1%, 5%, and 10% to examine its impact on b.

7.8.1.1   1% Increase in Standard Deviation e_1

Figure 7.2 depicts the IRFs of federal government debt to GDP, primary balance to GDP, and interest rate upon 1 percent increase on the standard deviation of Equation 4.5 at baseline parameter values. Figure 7.3 and Figure 7.4 depict the same IRFs at 0.01 unit of deviations. The y-axis of the graphs represent each variables' unit of deviation from its steady state value while x-axis represent the period of time. Hence at its basic, the IRFs show the trend of variables upon shock before the variables return to the steady state (Torres, 2013).
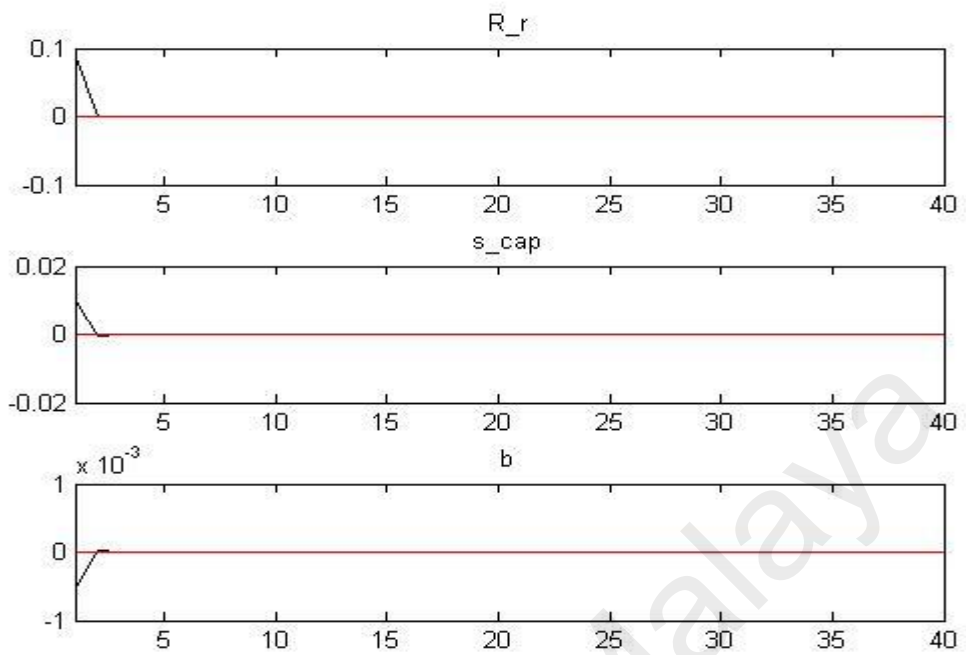
Figure 7.2: The IRFs of b, R^r, and $\hat{s}$ upon 1% Increase in e_1 (Baseline)
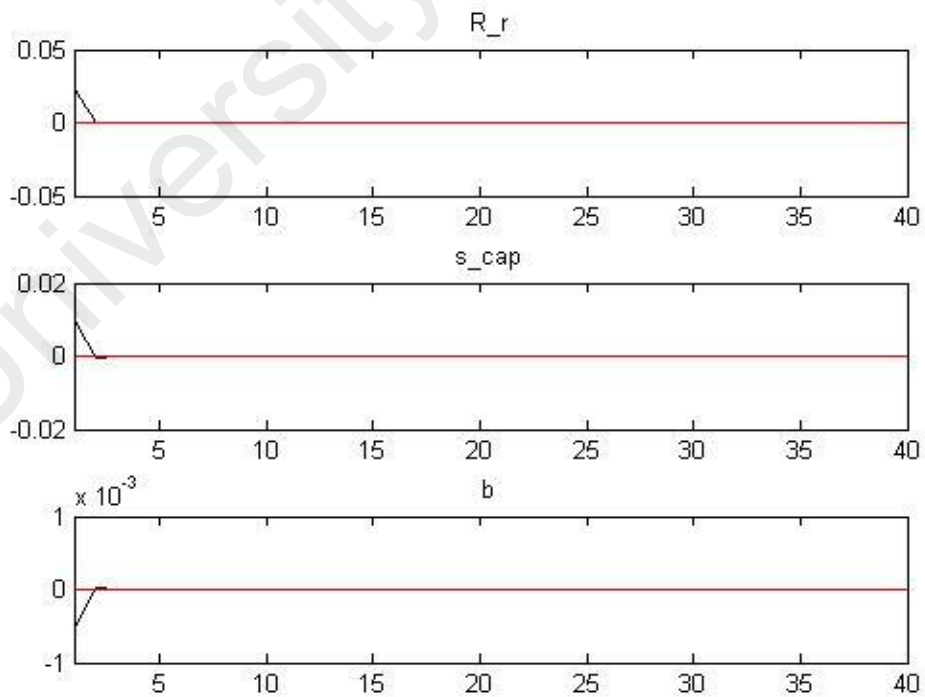
Figure 7.3: The IRFs of b, R^r, and $\hat{s}$ upon 1% Increase in e_1 (+0.01)
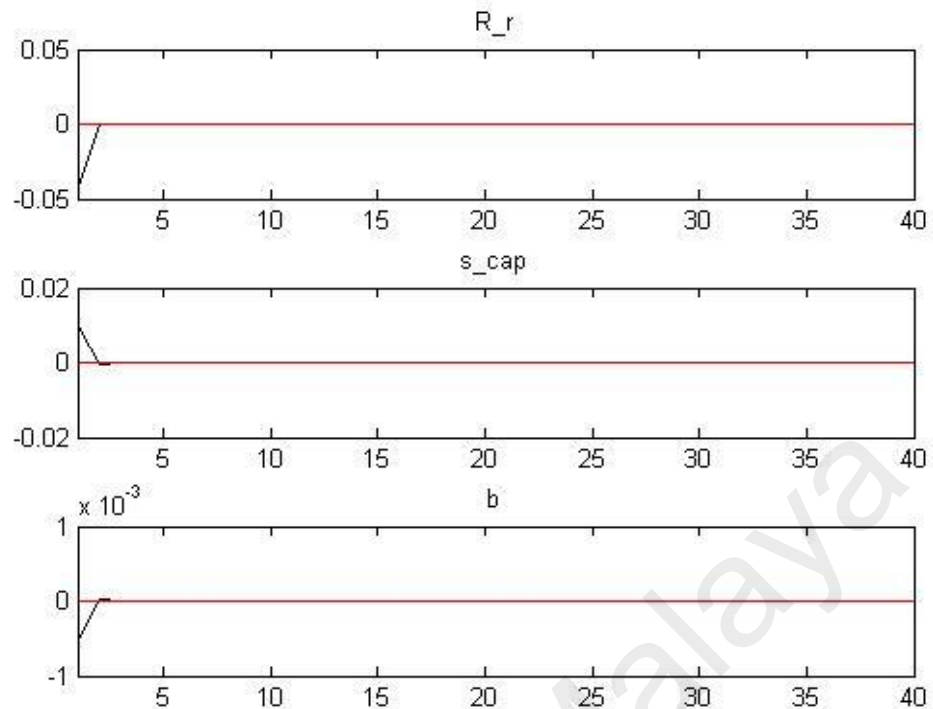
Figure 7.4: The IRFs of b, Rʳ, and ŝ upon 1% Increase in e₁ (-0.01)

As can be seen in all three figures, the federal government debt to GDP decreases by 0.05% upon impact before returning to its steady state. Although little, the major observation is that *waqf* financing public expenditure has an impact of decreasing federal government debt. This may be attributed to the fact that preference parameter of *waqf* contribution is higher in comparison to preference parameter of leisure. Even when the parameter values are reduced by 1%, debt to GDP still decreased before returning to its steady state. This also give evidence to the fact that the consideration of altruistic behaviour in households (cash *waqf* endowments) can impact debt. Plus, the reduction in debt coincides with the result from thematic analysis discussed in Section 7.2 and also the claim made by Çizakça (1998).

Also, similar rate of reduction despite deviations in parameter values may indicate that other strategies to further reduce debt, in addition to *waqf*, should be employed. This calls

for mixed strategies like that elaborated in Section 3.5. To reiterate, mixed strategies entail either mixing strategies between periods or variables. Regardless, further analysis would require another research which is out of this thesis's topic.

As for primary balance to GDP, all three figures show that it increases by 1% which is at the same rate of e_1 before returning to its steady state. This shows that *waqf* financing expenditure significantly impact primary balance to GDP as oppose to federal government debt to GDP. Hence, the inclusion of *waqf* in the Malaysian economy may also aid the persistent primary deficit that the country is experiencing. This coincides with the results of thematic analysis (Section 7.2) and findings of Mohd. Umar et al. (2012).

In terms of interest rate, huge changes are observed at different parameter values upon shock. The increase of interest rate upon shock at baseline parameter values is higher namely at 9% in comparison to +0.01 parameter values which is at 2%. These increases is intuitive as debt value decreases. After all, the Malaysian federal government debt also includes government bonds that move opposite with interest rate. However, the interest rate decreases by 4% at -0.01 parameter values despite the decrease in debt. One plausible reason can be derived from Equation 3.2. When the intertemporal discount factor decreases, it indicates that household value current utility more than future utility. Hence, consumption at time t is more than consumption at time $t+1$ which causes the right hand side value of Equation 3.2 to become smaller. Hence by extension, interest rate at time $t+1$ would reduce too. This is further justified by the fact that the interest rate decrease in -0.01 parameter value is higher than the interest rate increase of +0.01 parameter values.

Note that other variables namely consumption, labour, cash *waqf* endowment, capital, wage, rental rate of capital, investment, rate of return from cash *waqf*, final goods (GDP), cash *waqf* to GDP, total federal government expenditure, and total federal government

expenditure to GDP are not affected by the change in primary balance to GDP. This is why no IRFs for these variables were generated. Intuitively, this indicate three things. One, the amount of cash *waqf* endowment is not modelled as an AR(1) process. This is impossible to be done. As stated earlier, most SIRCs were unwilling to release the value of cash *waqf* fund in quarterly frequency, some did not provide them despite persistent enquiries, while others cannot disclose the values. Second, the 1% increase did not affect the other aforementioned variables because the value of shock is not significant enough. Otherwise, it is only a simple matter of economic fact for this modelled economy in that *waqf* return is not distortionary in nature. To confirm these intuitive claims, it is wise to shock the model with higher percentage values while retaining the deviations in parameter values.

7.8.1.2   5% Increase in Standard Deviation e_1

Figure 7.5 depicts the IRFs of federal government debt to GDP, primary balance to GDP, and interest rate upon 5 percent increase on the standard deviation of Equation 4.5 at baseline parameter values. Figure 7.6 and Figure 7.7 depict the same IRFs at 0.01 unit of deviations. Similar to Section 7.8.1.1, consumption, labour, cash *waqf* endowment, capital, wage, rental rate of capital, investment, rate of return from cash *waqf*, final goods (GDP), cash *waqf* to GDP, total federal government expenditure, and total federal government expenditure to GDP are not affected by the 5% shock. Hence, the earlier supposition that the value of shock is not significant enough can be rejected.
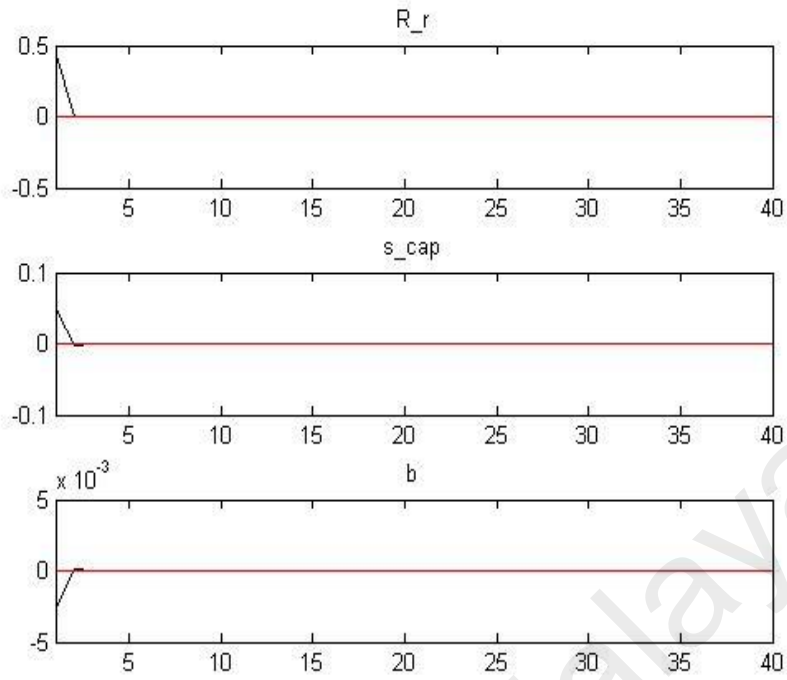
Figure 7.5: The IRFs of b, R^r, and $\hat{s}$ upon 5% Increase in e_1 (Baseline)
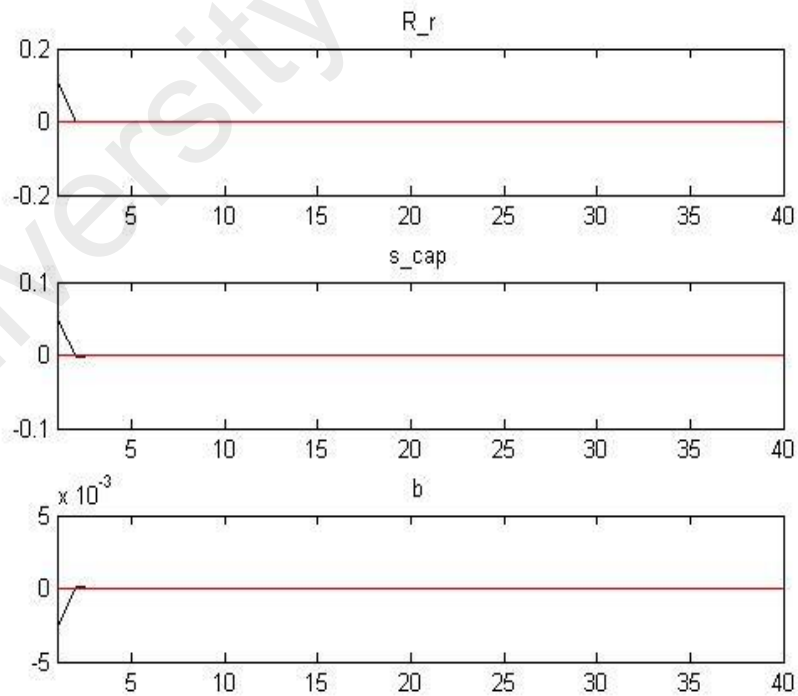
Figure 7.6: The IRFs of b, R^r, and $\hat{s}$ upon 5% Increase in e_1 (+0.01)
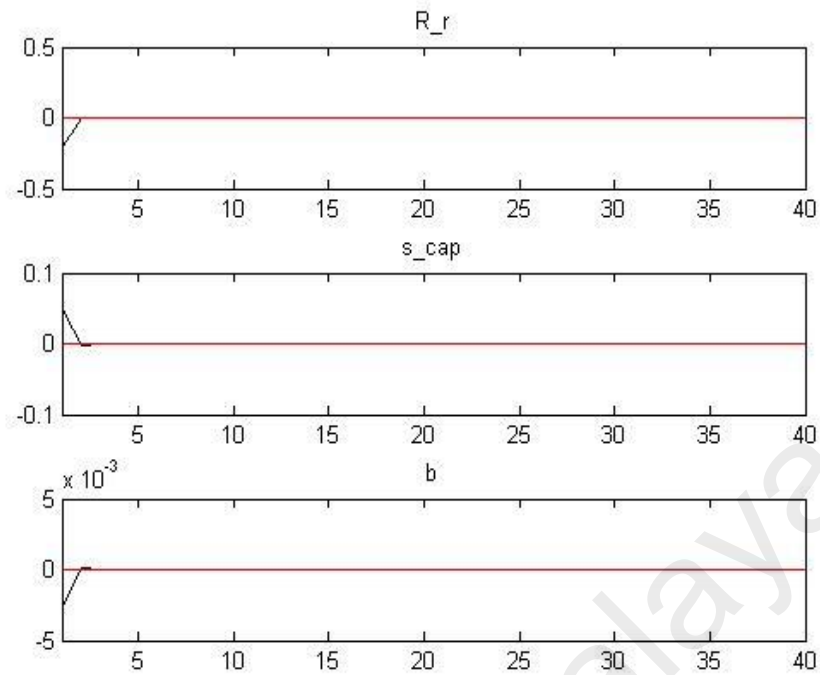
Figure 7.7: The IRFs of b, R^r, and $\hat{s}$ upon 5% Increase in e_1 (-0.01)

As can be seen in all three figures, the federal government debt to GDP decreases by 0.25% upon impact before returning to its steady state. Although may seem little, the important observation is that *waqf* financing public expenditure has an impact of decreasing federal government debt in all parameter value deviations. Moreover, similar to Section 7.8.1.1, it can be inferred that altruistic behaviour of households (through cash *waqf* endowments) can actually impact debt.

As for primary balance to GDP, all three figures show that it increases by 5% which is at the same rate of e_1 before returning to its steady state. This observation is similar to the observation in Section 7.8.1.1. Hence, it does not change the fact that *waqf* financing expenditure may also mitigate the persistent primary deficit that Malaysia is experiencing. In terms of interest rate, huge changes are observed at different parameter values upon shock; just like the findings in Section 7.8.1.1. This may be due to the household's preference on current utility as opposed to future utility.

214

7.8.1.3 10% Increase in Standard Deviation e_1

Figure 7.8 depicts the IRFs of federal government debt to GDP, primary balance to GDP, and interest rate upon 10 percent increase on the standard deviation of Equation 4.5 at baseline parameter values. Figure 7.9 and Figure 7.10 depict the same IRFs at 0.01 unit of deviations. Similar to the two previous sections, consumption, labour, cash *waqf* endowment, capital, wage, rental rate of capital, investment, rate of return from cash *waqf*, final goods (GDP), cash *waqf* to GDP, total federal government expenditure, and total federal government expenditure to GDP are not affected by the 10% shock. Hence, the claim that the value of shock is not significant enough can be rejected.
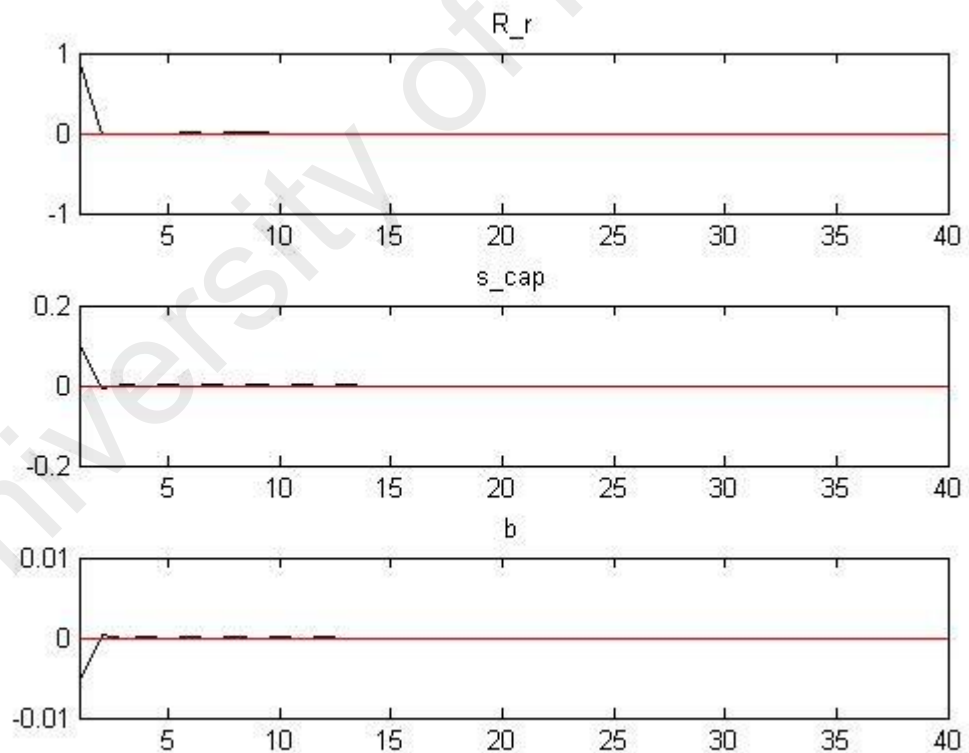
Figure 7.8: The IRFs of b, R^r, and $\hat{s}$ upon 10% Increase in e_1 (Baseline)
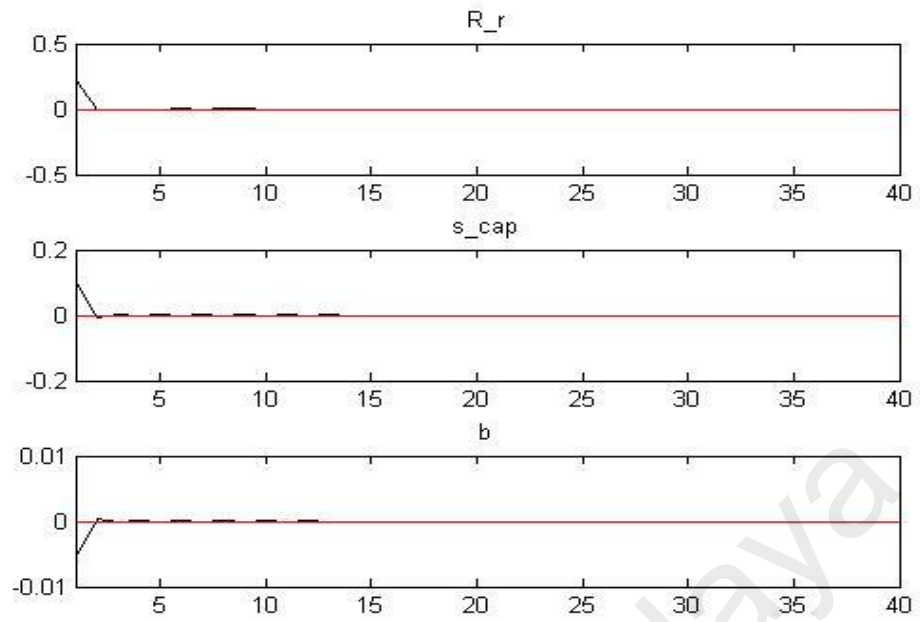
Figure 7.9: The IRFs of b, R^r, and $\hat{s}$ upon 10% Increase in e_1 (+0.01)
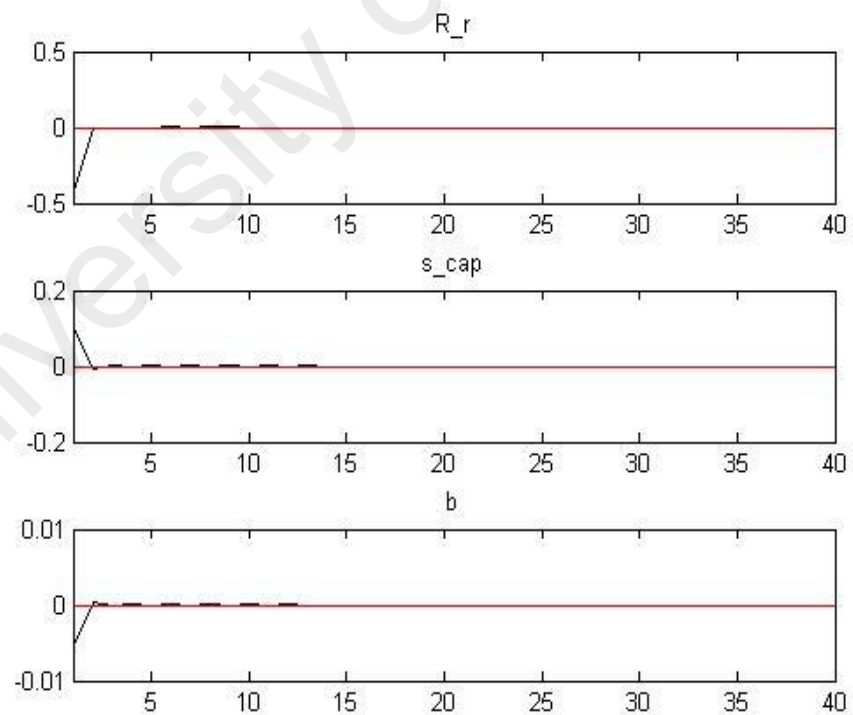
Figure 7.10: The IRFs of b, R^r, and $\hat{s}$ upon 10% Increase in e_1 (-0.01)

As can be seen in all three figures, the federal government debt to GDP decreases by 0.5% upon impact before returning to its steady state. Although may seem little, the important observation is that *waqf* financing public expenditure has an impact of decreasing federal government debt in all parameter value deviations. Therefore, this finding concur with the results from earlier shocks.

As for primary balance to GDP, all three figures show that it increases by 10% which is at the same rate of e_1 before returning to its steady state. This observation is similar to the observation in Section 7.8.1.1 and Section 7.8.1.2. Hence, it does not change the fact that *waqf* financing expenditure may also mitigate the persistent primary deficit that Malaysia is experiencing. In terms of interest rate, huge changes are observed at different parameter values upon shock; just like the findings in the previous two sections. To reiterate, this may be due to the households' preference on current utility as opposed to future utility.

7.8.2 Shock to Federal Government Expenditure to GDP

In order to add confidence to the result of decreased in debt, ascertain the result of Section 7.8.1, and ensuring that the theoretical model is correct, a shock to government expenditure is warranted. Specifically, e_2 is assigned the value of 1%, 5%, and 10% to examine its impact on debt to GDP. These shocks indicate an increase in total federal government expenditure to GDP. Should debt to GDP decrease despite of increase in total federal government expenditure to GDP, then inclusion of *waqf* in the economy is indeed of significance.

7.8.2.1 1% Increase in Standard Deviation e_2

Unlike the shock to primary balance to GDP, the shock to total government expenditure to GDP impacts all variables in the model. Figure 7.11 shows the IRFs of interest rate, rate of cash *waqf* return, primary balance to GDP, debt to GDP, total government expenditure, and total government expenditure to GDP at baseline parameter values. Figure 7.12 shows similar IRFs at +0.01 parameter values while Figure 7.13 at -0.01 parameter values.

In all the three figures, total government expenditure increases before returning to its steady state. This is called for since total government expenditure to GDP rises as e_2 is assigned a positive value. Due to the increase in expenditure, primary balance to GDP falls in all three figures before returning to its steady state. Unsurprisingly, the largest fall is at -001 parameter values to which the parameters of fiscal policy rule also fall. Despite this, debt to GDP observes a decrease which is made possible by the increase in rate of cash *waqf* return before returning to their steady state. In other words, *waqf* had become another alternative source of funding for expenditure instead of solely relying on borrowing. This decrease in debt also resonates with the findings of thematic analysis in Section 7.2 and Çizakça (1998).

Important to note is that the most pronounced decrease of debt to GDP is at +0.01 parameter values whereby the preference parameter of *waqf* contribution also increases. It further add evidence to the fact that altruistic behaviour (proxied by cash *waqf* contribution) has the effect of decreasing debt. Indeed, including altruism as another behaviour of household has shown that the third sector has impact on economic variables.
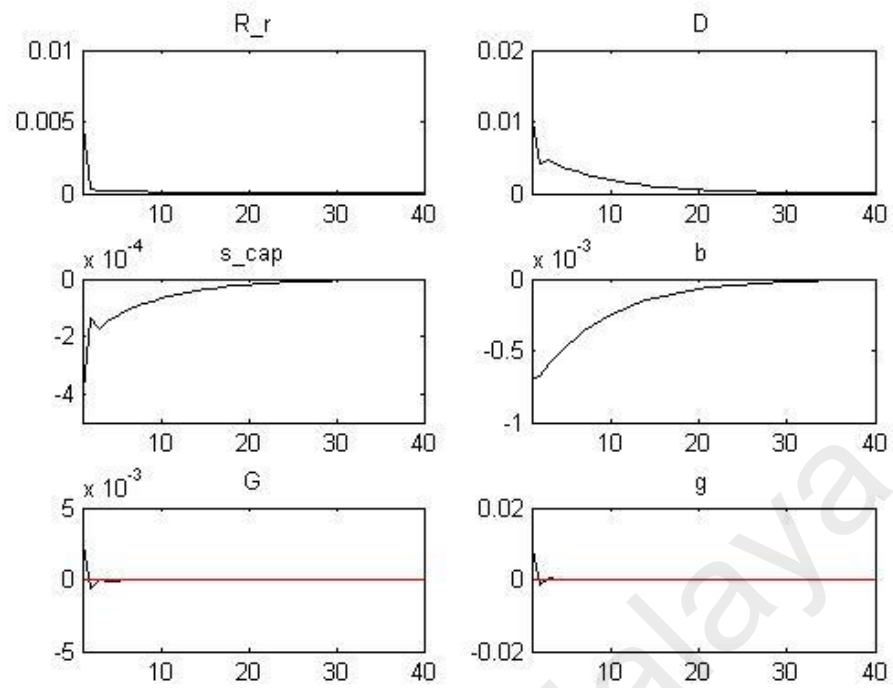
Figure 7.11: The IRFs of R^r, D, $\hat{s}$, b, G, and g upon 1% Increase in e_2 (Baseline)
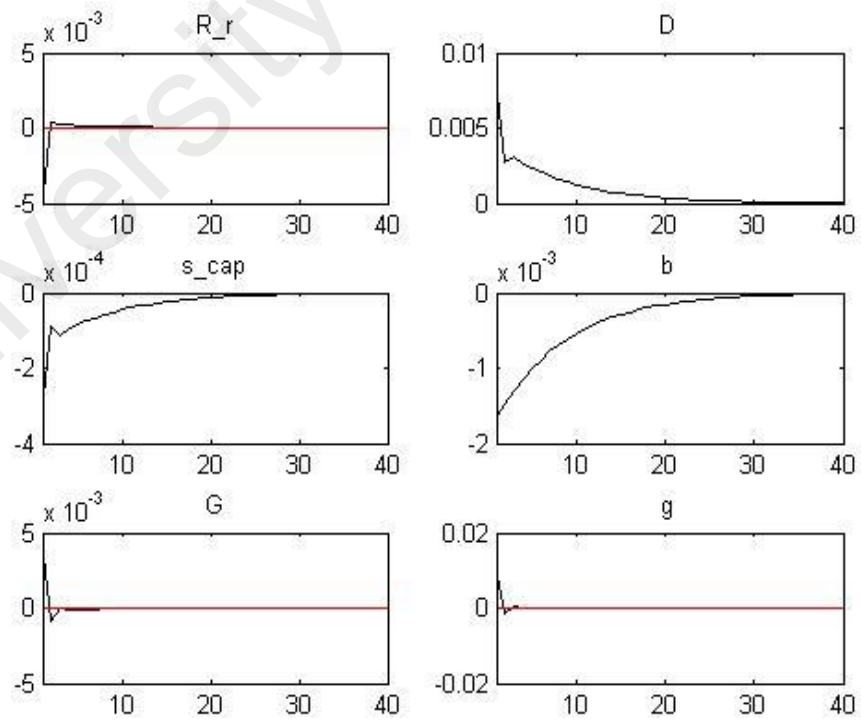
Figure 7.12: The IRFs of R^r, D, $\hat{s}$, b, G, and g upon 1% Increase in e_2 (+0.01)
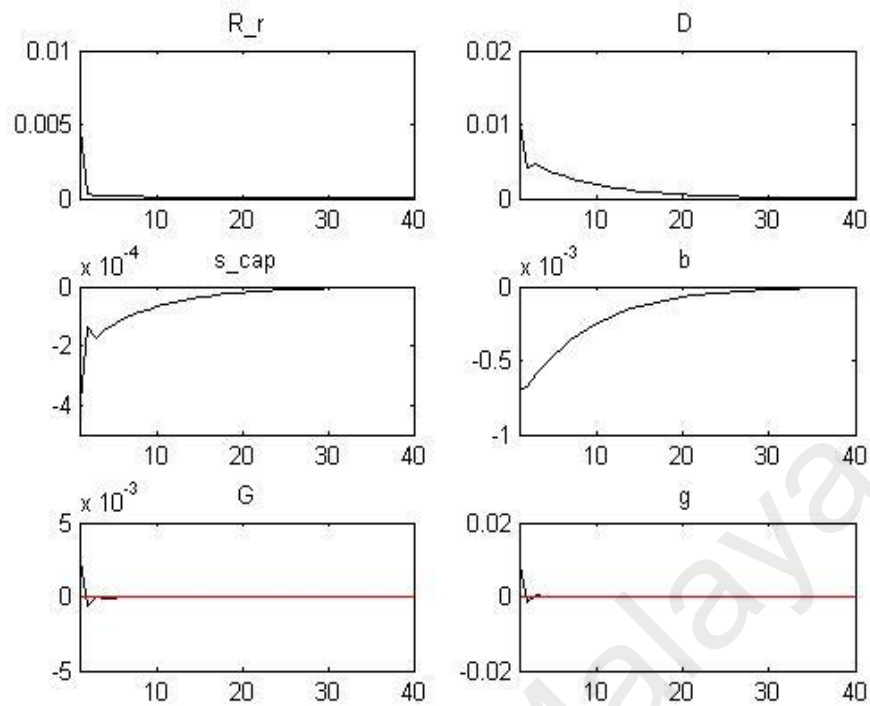
Figure 7.13: The IRFs of R^r, D, $\hat{s}$, b, G, and g upon 1% Increase in e_2 (-0.01)

The only variable in these three figures that are sensitive to the deviations in parameter values is interest rate. This is a similar observation with Section 7.8.1. As can be observe, the interest rate drops at +0.01 parameter values before returning to its steady state. Increase of parameter values mean that an increase is also observe in the intertemporal discount factor. This increase indicates that household value future utility more than current utility. Hence, the right hand side value of Equation 3.2 and Equation 3.1 should be higher due to the increase in the intertemporal discount factor and the higher weight given to future consumption. However, the right hand side value of Equation 3.2 is also constrained by the increase in depreciation rate of capital (see Equation 3.1); making the interest rate variable in Equation 3.2 to fall. In other words, the movement of interest rate is actually inversely proportional to the depreciation rate of capital.

Figure 7.14 to Figure 7.16 depict the rest of the IRFs namely labour, final goods, wage, rental rate of capital, consumption, cash *waqf* contribution, investment, capital, and cash *waqf* to GDP. In all three parameter value cases (baseline, +0.01, and -0.01), only labour and rental rate of capital rise before returning to their steady state upon shock. The other variables drop before returning to its steady state. On the other hand, investment drops then rises for a short while before returning to its steady state.
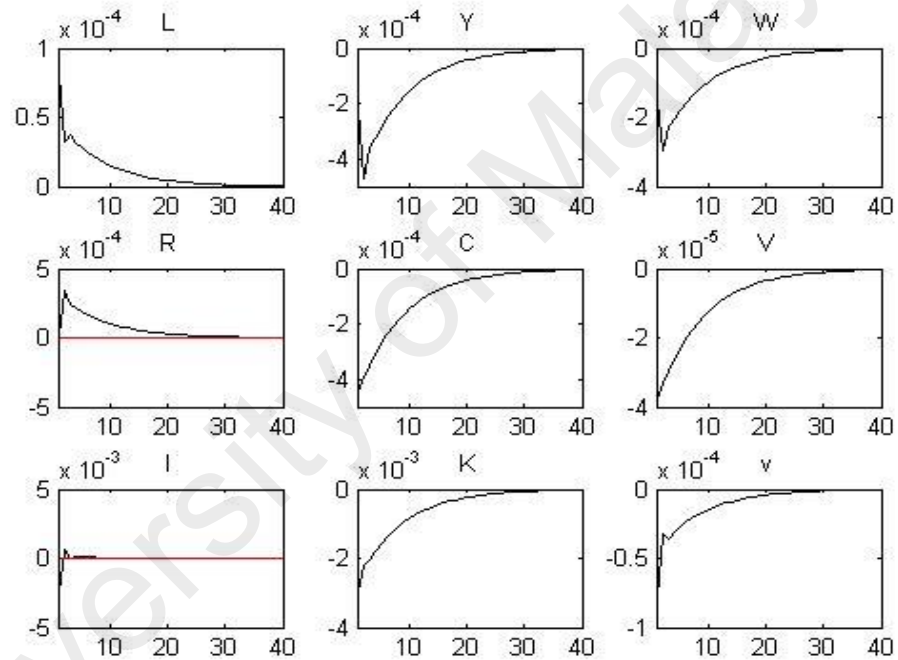
Figure 7.14: The IRFs of L, Y, W, R, C, V, I, K, and v upon 1% Increase in e_2 (Baseline)
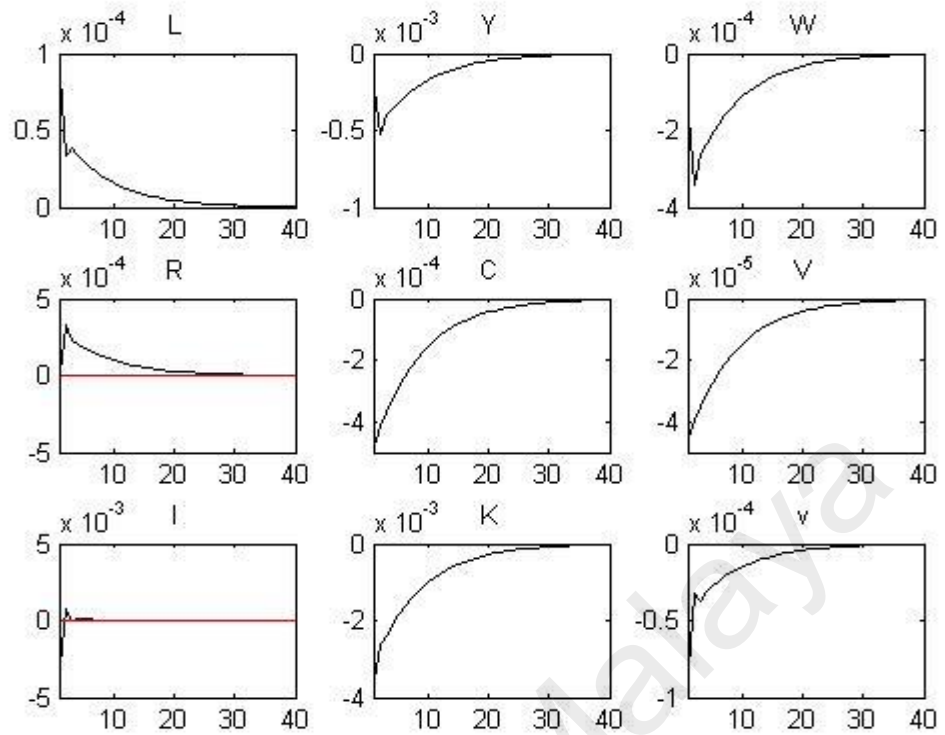
Figure 7.15: The IRFs of L, Y, W, R, C, V, I, K, and v upon 1% Increase in e₂ (+0.01)
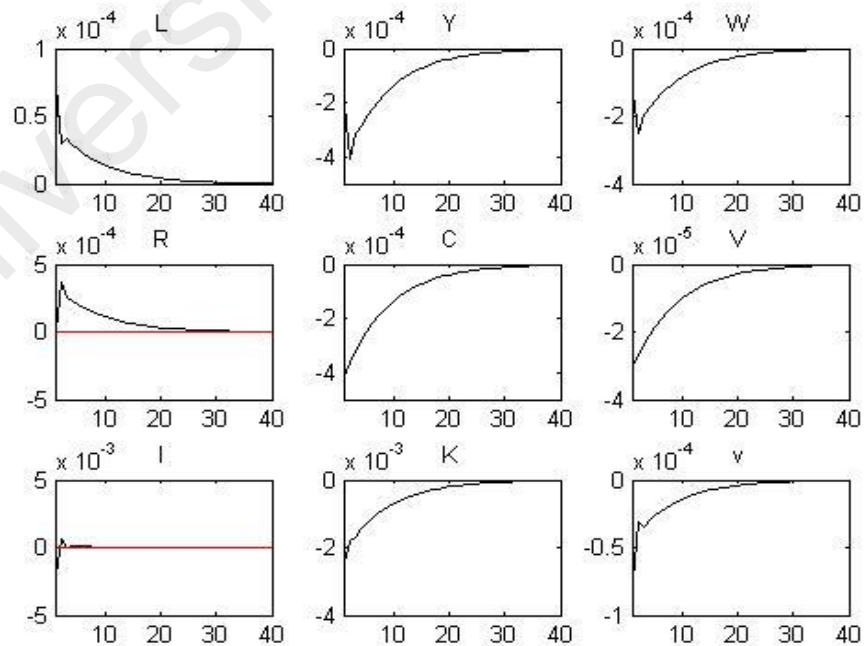
Figure 7.16: The IRFs of L, Y, W, R, C, V, I, K, and v upon 1% Increase in e₂ (-0.01)

Albeit the increase in total government expenditure due to shock, final goods still decrease due to decrease in investment, consumption, and cash *waqf* contribution. However, this decrease in final goods is not alarming because as has been seen earlier, debt to GDP also decreases. In other words, the retraction in GDP is still manageable as debt did not rise. As a matter of fact, there are more employment opportunities as evident in the rise of labour. Naturally, the rise in labour would cause a fall in wage as per the law of demand and supply. Similarly, the rise in the rental rate of capital is due to the fall in capital. The latter is because households need to portion their budget for cash *waqf* too; the aspect of altruism to which many macroeconomic models did not consider. Along the same lines, the decrease in cash *waqf* contribution may be attributed to the decrease in wage.

Important to observe is that decrease in cash *waqf* contribution did not cause debt to GDP to increase. This is because cash *waqf* return and not cash *waqf* itself that is used to finance government public expenditure. In other words, the decrease in cash *waqf* contribution is of secondary matter as long as the return from cash *waqf* is sufficiently obtain.

7.8.2.2 5% Increase in Standard Deviation e$_2$

Increasing the shock of total government expenditure to GDP also impacts all variables in the model. Figure 7.17 shows the IRFs of interest rate, rate of cash *waqf* return, primary balance to GDP, debt to GDP, total government expenditure, and total government expenditure to GDP at baseline parameter values. Figure 7.18 shows similar IRFs at +0.01 parameter values while Figure 7.19 at -0.01 parameter values.

In all the three figures, total government expenditure increases before returning to its steady state. Due to the increase in expenditure, primary balance to GDP falls in all three figures before returning to its steady state. Despite this, debt to GDP observes a decrease which is made possible by the increase in rate of cash *waqf* return before returning to their steady state. These findings are similar to that in Section 7.8.2.1, Section 7.2, and Çizakça (1998).
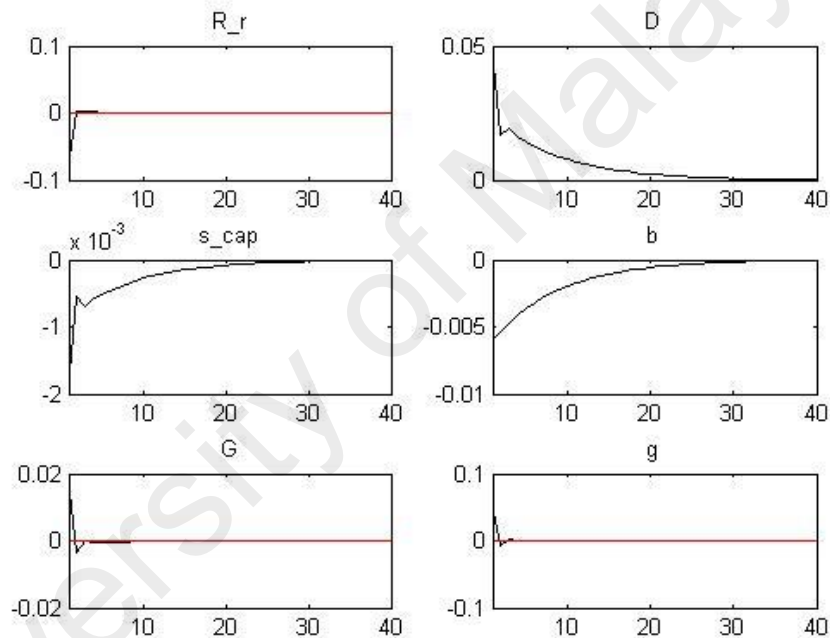
Figure 7.17: The IRFs of R^r, D, ŝ, b, G, and g upon 5% Increase in e$_2$ (Baseline)
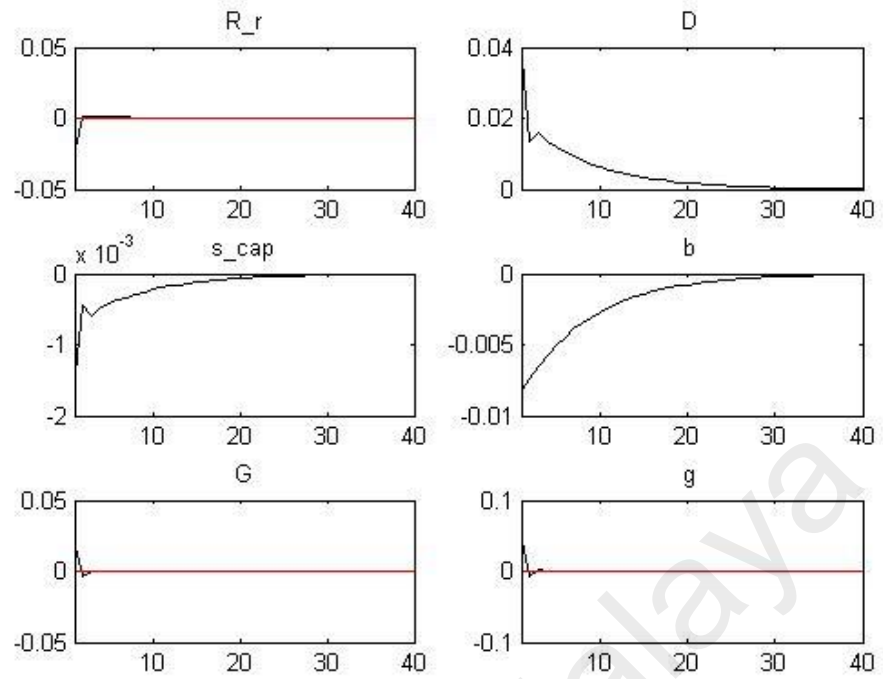
Figure 7.18: The IRFs of Rʳ, D, ŝ, b, G, and g upon 5% Increase in e₂ (+0.01)
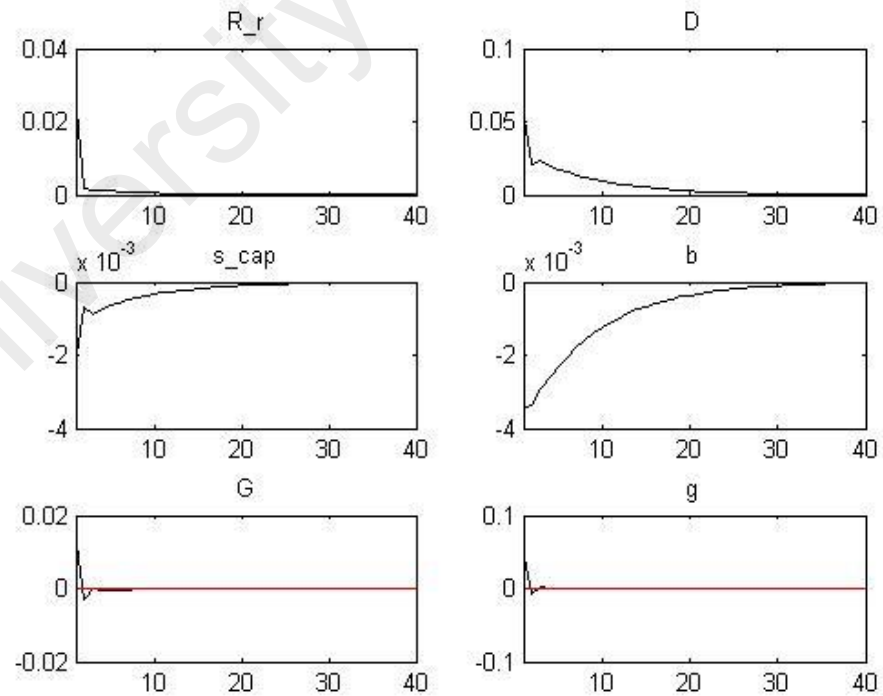
Figure 7.19: The IRFs of Rʳ, D, ŝ, b, G, and g upon 5% Increase in e₂ (-0.01)

The only variable in these three figures that are sensitive to the deviations in parameter values is interest rate. As such, this observation is similar to the movement of interest rate when 1% shock is induced. Hence, the movement of interest rate is indeed inversely proportional to the depreciation rate of capital.

Figure 7.20 to Figure 7.22 depict the rest of the IRFs namely labour, final goods, wage, rental rate of capital, consumption, cash *waqf* endowment, investment, capital, and cash *waqf* to GDP. In all three parameter value cases (baseline, +0.01, and -0.01), only labour and rental rate of capital rise before returning to their steady state upon shock. The other variables drop before returning to its steady state. On the other hand, investment drops then rises for a short while before returning to its steady state. These observations are also similar with the observations in Section 7.8.2.1. Therefore, explanations for the movement of IRFs would remain the same as in Section 7.8.2.1
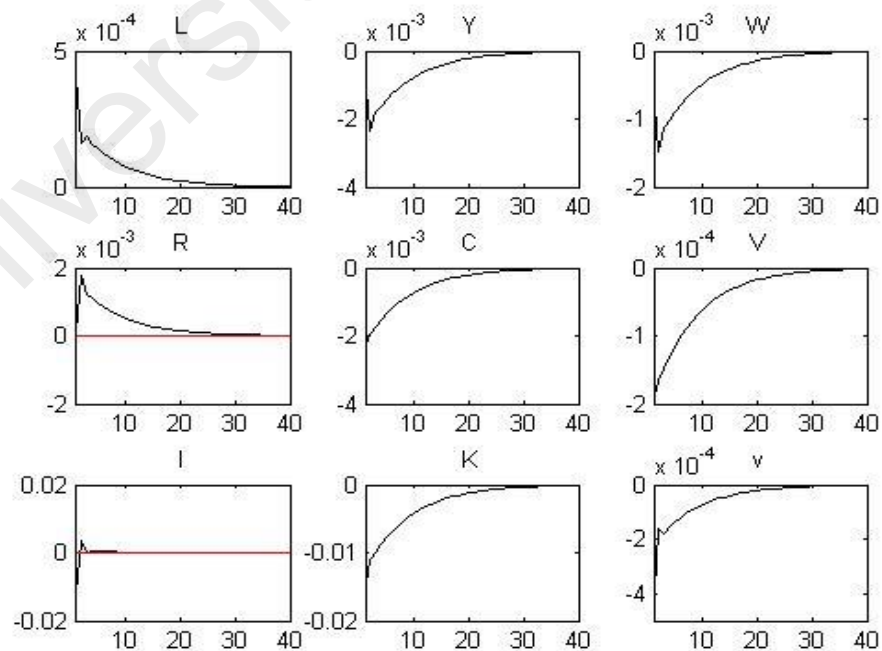
Figure 7.20: The IRFs of L, Y, W, R, C, V, I, K, and v upon 5% Increase in e$_2$ (Baseline)
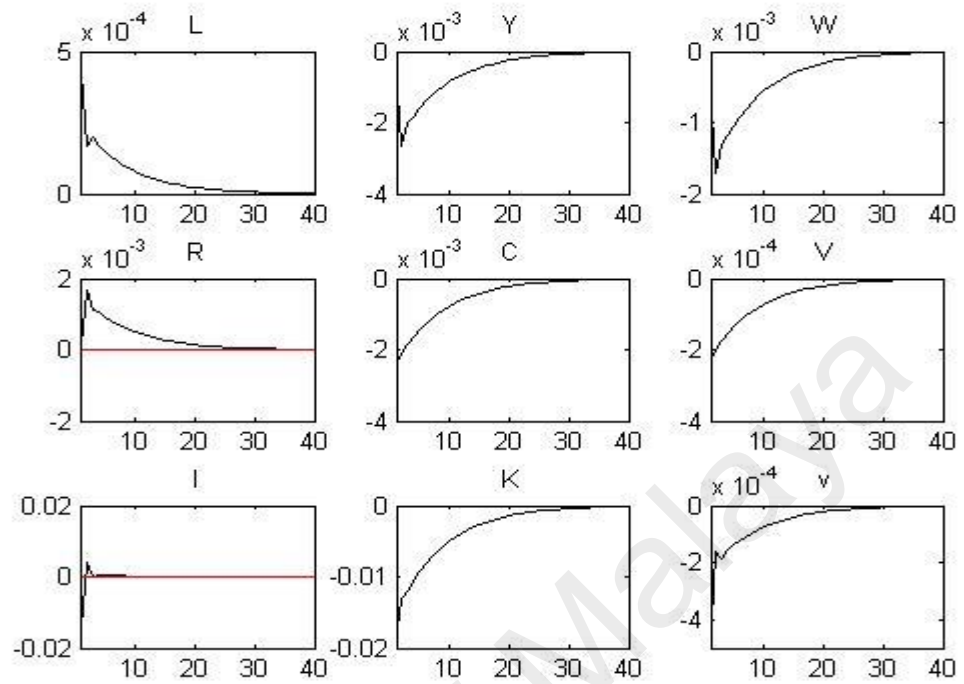
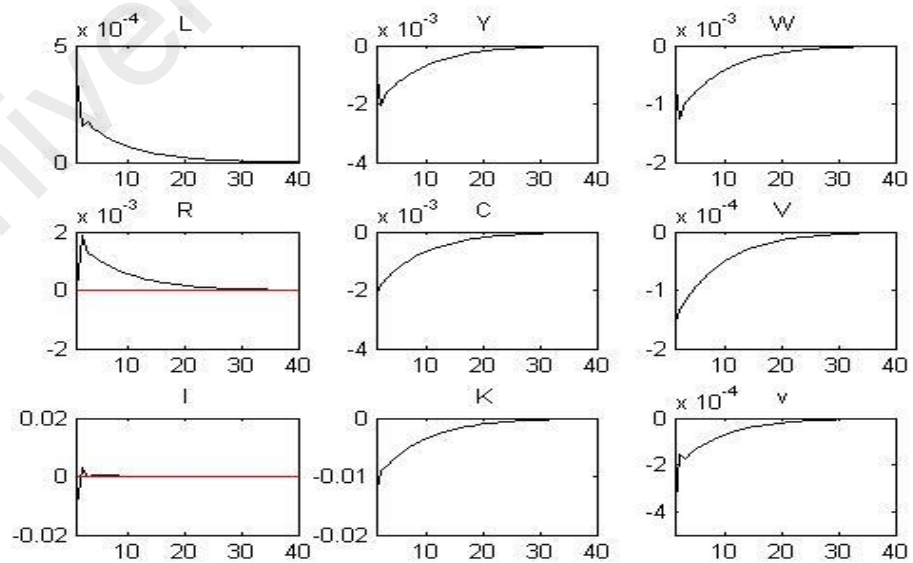**Figure 7.21: The IRFs of L, Y, W, R, C, V, I, K, and ν upon 5% Increase in e₂ (+0.01)**

Figure 7.22: The IRFs of L, Y, W, R, C, V, I, K, and ν upon 5% Increase in e₂ (-0.01)

7.8.2.3   10% Increase in Standard Deviation e_2

Further increasing the shock of total government expenditure to GDP also impacts all variables in the model. Figure 7.23 shows the IRFs of interest rate, rate of cash *waqf* return, primary balance to GDP, debt to GDP, total government expenditure, and total government expenditure to GDP at baseline parameter values. Figure 7.24 shows similar IRFs at +0.01 parameter values while Figure 7.25 at -0.01 parameter values.

In all the three figures, total government expenditure increases before returning to its steady state. Due to the increase in expenditure, primary balance to GDP falls in all three figures before returning to its steady state. Yet again, debt to GDP observes a decrease which is made possible by the increase in rate of cash *waqf* return before returning to its steady state. Hence these findings repeat that of Section 7.8.2.1, Section 7.8.2.2, Section 7.2, and Çizakça (1998).
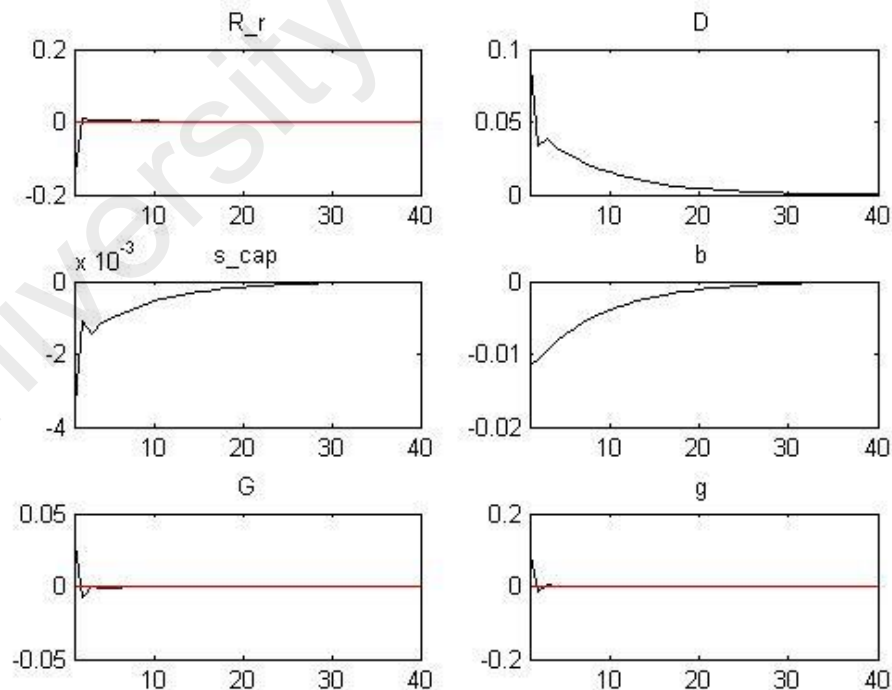
**Figure 7.23: The IRFs of R^r, D, $\hat{s}$, b, G, and g upon 10% Increase in e_2 (Baseline)**
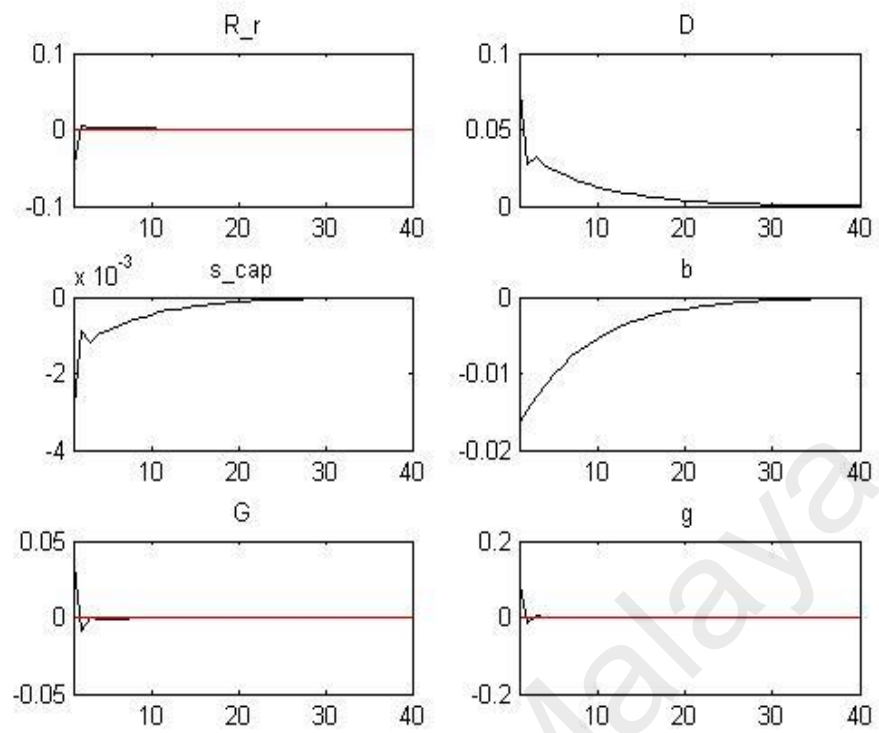
Figure 7.24: The IRFs of R^r, D, ŝ, b, G, and g upon 10% Increase in e$_2$ (+0.01)
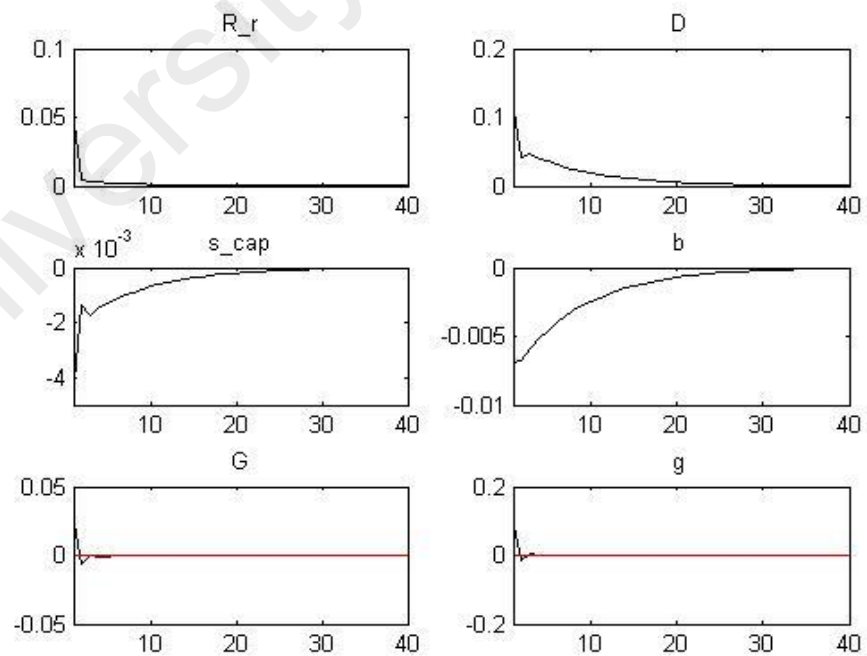
Figure 7.25: The IRFs of R^r, D, ŝ, b, G, and g upon 10% Increase in e$_2$ (-0.01)

Just like when the economy were shocked at 1% and 5%, interest rate is the only variable that is sensitive to the deviations in parameter values. This is because at +0.01 parameter values, the intertemporal discount factor also increases which gives more weight to future utility. This inadvertently cause the interest rate to fall.

Figure 7.26 to Figure 7.28 depict the rest of the IRFs namely of labour, final goods, wage, rental rate of capital, consumption, cash *waqf* endowment, investment, capital, and cash *waqf* to GDP. In all three parameter value cases (baseline, +0.01, and -0.01), only labour and rental rate of capital rise before returning to their steady state upon shock. The other variables drop before returning to its steady state. On the other hand, investment drops then rises for a short while before returning to its steady state. These observations are also similar with the observations in Section 7.8.2.1 and Section 7.8.2.2. Therefore, explanations for the movement of IRFs would remain the same as in those two previous sections.
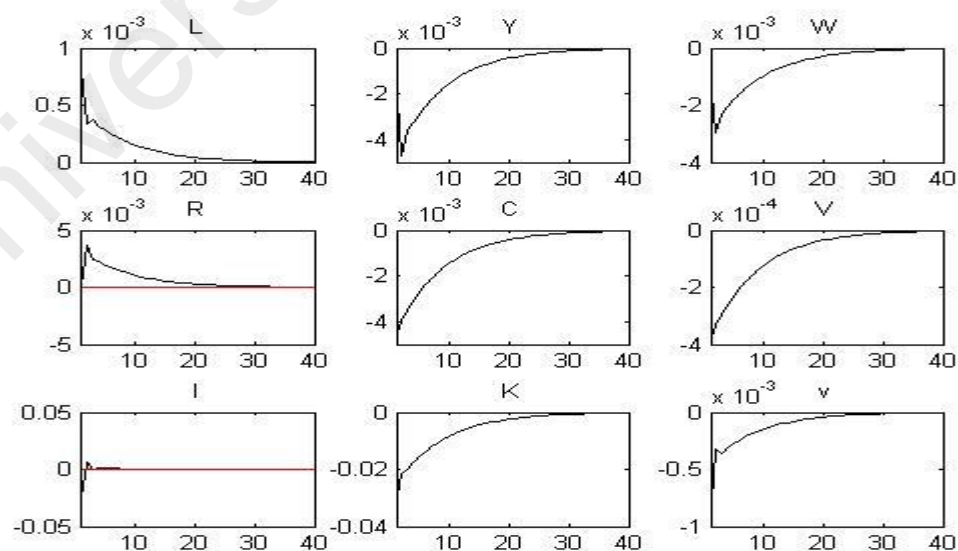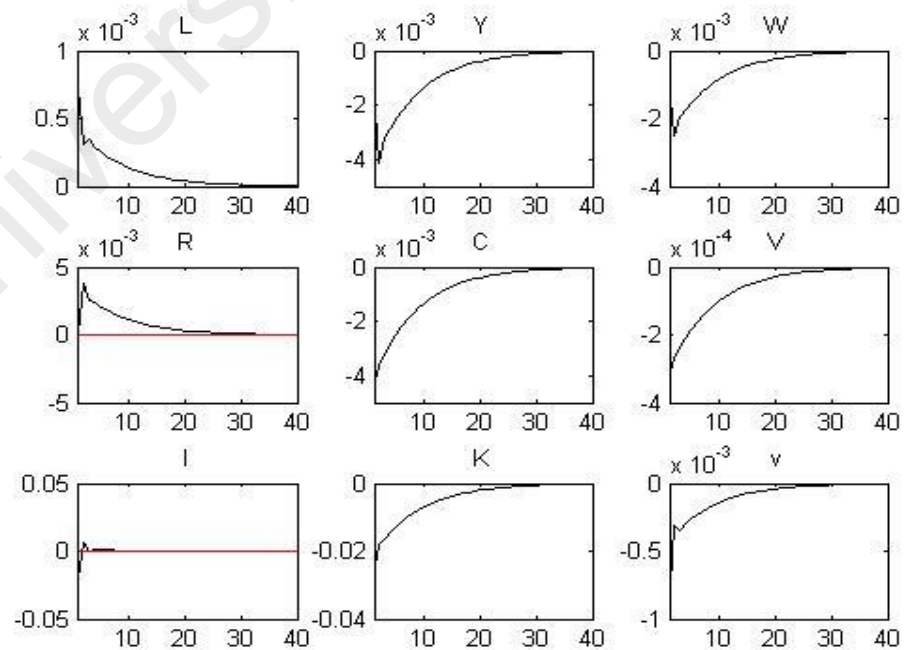

Figure 7.26: The IRFs of L, Y, W, R, C, V, I, K, and v upon 10% Increase in e_2 (Baseline)
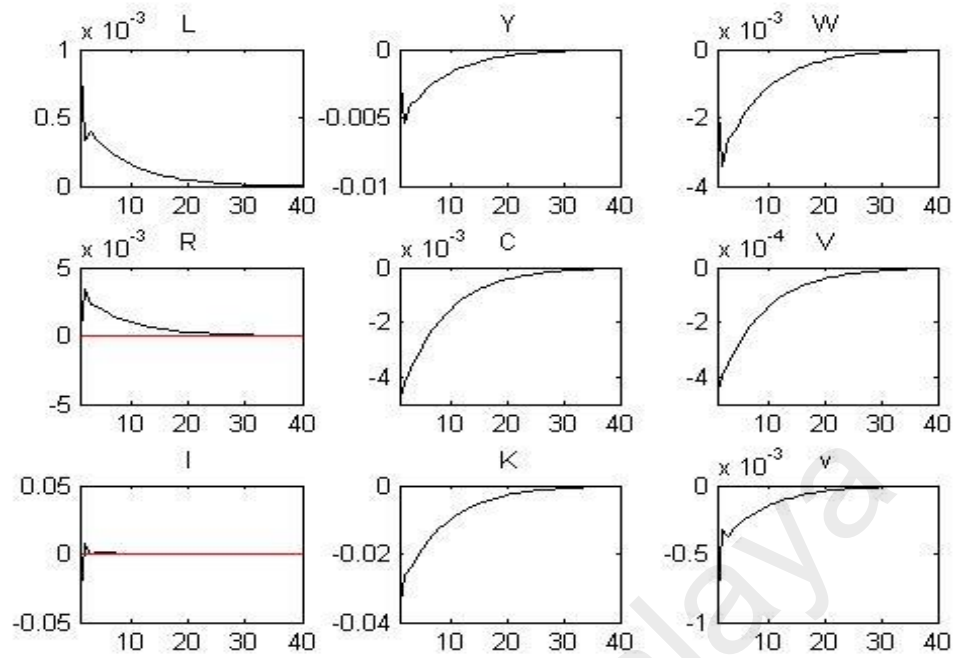
Figure 7.27: The IRFs of L, Y, W, R, C, V, I, K, and v upon 10% Increase in e₂ (+0.01)

Figure 7.28: The IRFs of L, Y, W, R, C, V, I, K, and v upon 10% Increase in e₂ (-0.01)

7.9 Conclusion

This chapter had demonstrated that *waqf* financing Malaysian federal government public expenditure decreases federal government debt to GDP. This serves as an answer to RQ 4 which corresponds to RO 3 and rejects H_1. The result is attainable and rational because the altruistic behaviour of households are taken into account in the theoretical model. In addition, *waqf* also has the potential to create primary surplus because public expenditures are catered by the return of cash *waqf*. This is evident based on the fact that the shocks impact primary balance more than debt. Both of these findings were also supported by the interviewees' perspective and findings from the literature. More than that, this chapter has showed that *waqf* is not anachronistic but is able to acquire a significant role in modern economy.

CHAPTER 8: CONCLUSION

8.1 Introduction

Chapter 8 links the qualitative results of RO 1, RO 2, and a minor part of RO 3 with the quantitative results from the major part of RO 3. This is done by offering a critical summary and interpretation of both the qualitative and quantitative results before discussing how the quantitative results generalise the qualitative results. All of these are discussed in Section 8.2. Next, research limitations and research implications are presented in Section 8.3 and Section 8.4 respectively. The research limitations identify the constraints that this study faced while the research implications accentuate the study's significance. Meanwhile, Section 8.5 lists the ideas that can carry this research further. Finally, this chapter and thesis concludes in Section 8.6.

8.2 Connecting and Interpreting the Qualitative and Quantitative Strands

In theory, *waqf* financing public expenditure is doable based on the fact that it is allowed from the *Shari'ah* standpoint, was implemented in the past, and is encouraged by the federal government. This simultaneously answer RQ 1. Its *Shari'ah* permissibility indicates that *waqf* is an instrument capable of growth following the economic age it is in. Just like during the Ayyubid and Ottoman Dynasty, *waqf* was able to achieve its zenith in those eras while still retaining its principles. This is made possible due to the *ijtihad* process and altruistic realisations. The Malaysian federal government also recognised this and allocated part of the fiscal budget for *waqf irsod*.

However, discovering that *waqf* financing public expenditure is viable in practice is not enough. Thus, RQ 2 was laid out to identify issues that may arise from this application within the context of Malaysian *waqf*. RQ 3 was then designed to address these issues and to recommend a suitable model for *waqf* financing public expenditure in Malaysia.

Issues that directly pertain to *waqif, mawquf, waqf* trustee, financing strategy, and *mawquf 'alaih* were given due diligence because these particular issues are the building blocks for the model. It is essential that these RQs are answered so that this idea can be put into real practice.

The first issue is from the aspect of legality. *Waqf* law lays the foundation and gives permission to *waqf* financing public expenditure to operate. Majority of state laws do not contain stipulations that allow private sector to manage *waqf*. This can affect *waqf* financing public expenditure negatively because SIRC will need the skills and experience that private sector possesses. Among the skills that are needed which SIRCs lack are ensuring the perpetuity of *mawquf* and generating returns from *mawquf* which also requires knowledge in Islamic finance. This inadvertently relates to the management issue of *waqf*. In addition, most Malaysian states do not promulgate specific *waqf* enactment. This may cause confusion in the execution and management of *waqf* for public expenditure which is of fiscal magnitude.

To address these legal issues, partial centralisation was recommended. Firstly, instead of categorising Malaysian *waqf* into *waqf 'am*, *waqf khas*, and *waqf musytarak*, Malaysian *waqf* should be categorised into private *waqf*, religious *waqf*, and philanthropic *waqf*. This is so that the first two categories of *waqf* may remain under the trusteeship of SIRCs, while the third is placed under YWM. This idea is rational for two reasons. First, states will not completely lose its role as the trustee of *waqf* and its freedom to stipulate their own *waqf* laws. Second, a single consistent law for *waqf* financing public expenditure can be promulgated as the Federal Territories *Waqf* Act. Recall that *waqf* financing public expenditure is a constituent of philanthropic *waqf*.

The second issue stems from the aspect of management. Human resources in SIRCs faced insufficient know-how and broad job scope which will cause the execution of *waqf*

for public expenditure to be inefficient. As a result, heightened bureaucracy will occur which in turn breeds public dissatisfaction. The lack of transparency aggravates the problem further. These facts further stress the need of Federal Territories *Waqf* Act and for YWM to take charge. To address the insufficient know-how and broad job scope, YWM can collaborate with an Islamic financial firm. The Islamic financial firm may advice YWM with regards to maintaining and managing the perpetuity of *mawquf*. It was also suggested by the interviewees that *waqf* deeds detailing on the purpose of cash *waqf* endowment and its management should be exercised. Both the firm and YWM may also collaborate to produce intermittent reports on *waqf* activities. All of these measures should be able to garner public trust.

Corresponding to this is the third issue of *waqf* which is financial strategy. It was found that SIRCs tend to adopt traditional strategies as opposed to the private sector. Without strategies that can optimise returns, *waqf* for public expenditure may not be sustainable in the long run. Results from semi-structured interviews showed that cash *waqf* is the appropriate form of *mawquf* and investment of cash *waqf* in Islamic unit trust fund is a measure to be taken to ensure its perpetuity. Hence, the collaborating Islamic financial firm will actually be an Islamic unit trust firm. The Islamic unit trust firm may decide on the portfolio of securities and shares, convert them into an Islamic unit trust fund, get *Shari'ah* certification and authorisation from the SC, and ultimately manage the risk of that portfolio. YWM on the other hand, could manage the process of receiving and disbursement of cash *waqf* endowment as well as transcribing *waqf* deeds.

Contemplation and deliberation of all these factors translate into the model for *waqf* financing public expenditure depicted in Figure 6.4. However, it must be reminded that *waqf* can only assume a complementary role in the Malaysian economy. Hence, whenever

there is a loss from *waqf* returns up to the point where the original value of *mawquf* is eroded, the federal government must compensate that loss.

On the other hand, studying the impact of the *waqf* application on debt is vital in demonstrating evidence for the significance of *waqf* financing public expenditure. Both the qualitative and quantitative results point to a decrease in debt. In fact, both strands showed that primary deficit can be reduced too. Quantitative analysis had further shown that increase in *waqf* returns has an impact of reducing debt to GDP more than it reduces primary deficit. The persistence of debt to GDP in its movement towards the steady state value indicate that *waqf* returns has a significant impact on reducing debt. All in all, RQ 4 has been answered whereby *waqf* financing Malaysian federal government public expenditure has an impact of reducing federal government debt.

The theoretical model employed to study this impact on debt (Section 7.4) was initially generated from the public *waqf* economy (Figure 2.8) and the standard Neoclassical model. However, it also coincides with the qualitative findings of Chapter 6. Specifically, the general public as the *waqif* is represented by households, the portfolio of securities in the Islamic *waqf* unit trust fund primarily consist of that from firms, and YWM is the representative of the Malaysian federal government. Note that beneficiaries of cash *waqf* at its core, is also a household member. The approach of the theoretical model indicated that household took its own initiative to invest its endowed cash *waqf* when it is the responsibility of YWM and the Islamic unit trust firm to do so. In addition, the theoretical model also did not show the flow of Islamic unit trust returns to the beneficiaries.

Refer to Figure 8.1. In Chapter 6, the endowed cash *waqf* by household is being entrusted to YWM, the federal government body for *waqf*. This is step one. Islamic unit trust firm through a joint collaboration with YWM then decides on a portfolio of investment that primarily consist of equities and securities of firms. After this has been

decided, only then does the cash *waqf* be invested in the said Islamic unit trust fund. This is step two. Returns from the Islamic unit trust fund are then channelled back to YWM. This is step three. YWM will then disburse the returns according to the specified beneficiaries which are ultimately households. This is step four.
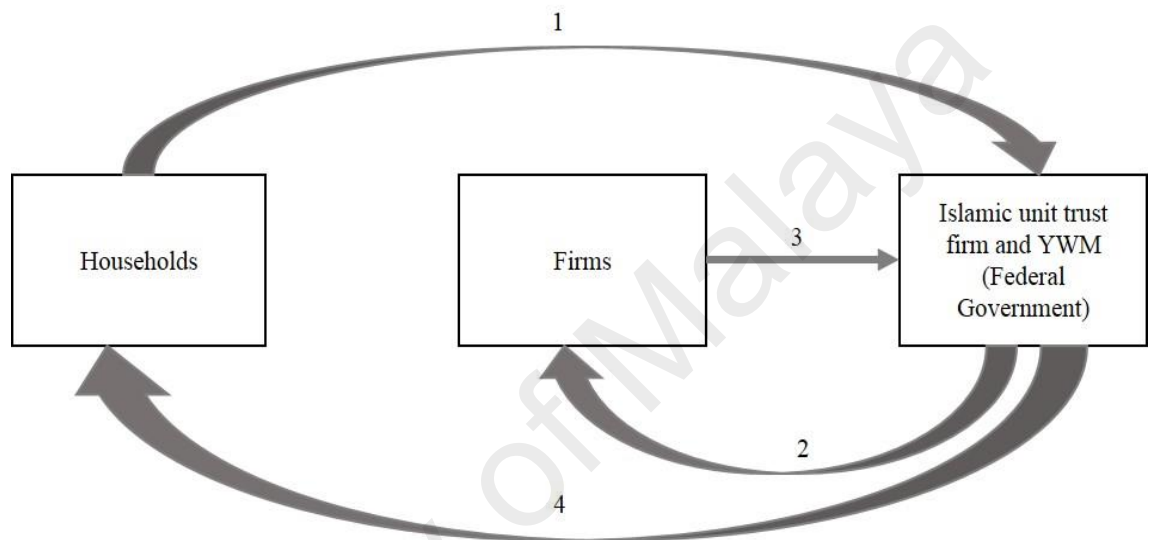
Figure 8.1: The Flow of Cash *Waqf* and Its Return

Now although the theoretical model did not depict an exact flow of cash *waqf* and its investment, the theoretical model is still valid because the federal government's budget constraint (Equation 4.2) contains the returns from firms ($v_t D_t$), while firm's production function (Equation 5.1) contains cash *waqf* (V_t). The beneficiaries on the other hand, are translated in Equation 4.1 as government expenditure (G_t). Moreover, the theoretical model was built to depict a simplified version of any economy which is the norm in the literature of DSGE model. It has already been stated earlier that the federal government's responsibility as a *mutawalli* is to spend the returns of cash *waqf* on specified public expenditures only.

8.3   Research Limitations

The main limitation of this thesis is that data on cash *waqf* were not able to be systematically obtained from most SIRCs. As was repeatedly mentioned, most SIRCs were unwilling to release the value of *waqf* fund in quarterly frequency which is a must for estimation purposes. Some did not provide the data despite persistent enquiries, while others cannot disclose the values. Still, this thesis has demonstrated the fact that simulation can still be carried out using proxy of cash *waqf* returns. This is because in principle, the value of *mawquf* must remain in perpetuity and only returns are allowed to change.

Secondly, the proposed idea of *waqf* financing public expenditure heavily depends on the willingness of the general public to endow *waqf*. After all, *waqf* is a third sector component; hence, it is a voluntary source of revenue. Academician F stated that this can be a challenge in and of itself for the following reason:

One of the big challenges you'll face in Malaysia now is whenever you ask people to make *waqf* of certain thing, they will say but that is government role. Trying to get people to give money to universities, they'll say this is government role.

However, other interviewees are optimistic that *waqf* contribution will rise due to conscious practice of Islam, the culture of giving that the federal government is attempting to foster, and studies done on *waqf*. Academician B is of the opinion that, "And seeing the way things are, I'm sure the value [of *waqf*] will rise. Because one thing is *alhamdulillah*, Muslims are becoming more conscious, aware of the need of their deen, religion". Academician E had also argued the same, "I think that one [*waqf*] will increase because people will always look at the ways to do *infaq* (donation), how to make *sadaqah* (donation), how to increase spending in the way of ALLAH…". Although these points only argue the altruistic motives of Muslims, non-Muslims also obviously have altruistic

tendencies. Government Official D had given a talk about *waqf* in one of the public universities in Malaysia and was asked by a non-Muslim, "I am intrigued with the concept of *waqf*. Can I as a non-Muslim endow *waqf* too?" Hence, it is important that the non-Muslim public are exposed to the concept of *waqf* too. The key is to educate the public that *waqf* endowments are not necessarily for religious purposes but also for the common good that is in line with Islam. In addition, learning the large role of *waqf* in economics through its implementation can greatly shift the public perception too.

Indeed, Academician G and Academician B observed a rise in research conducted about *waqf*. Rise in research points to a rise in public awareness. In the words of Academician G:

[Yes], I do believe [that the value of *waqf* will rise] and if you see the trend today, in the past I don't see much research paper and conference presentation on *waqf*. Recently I see a lot of people trying to contribute and present papers on *waqf*. So it's becoming very good attraction as an area of research.

Even you writing in *waqf* to me is good news. Meaning you are so conscious about that there is a need for this thing to us as Muslims. So the awareness, looking at the number of literature on *waqf*, conferences on *waqf*, interest in *waqf*, for sure is on the rise. Just go and check on people's thesis doing like you doing the thesis on *waqf*, look at the number of conferences worldwide, look at those interest that are developing.

This awareness should be further heightened by encouragement from the federal government. As pointed out by Academician C, "Yes! Because we are heading towards the culture of giving. The government is giving support [for *waqf*]. There is an inclination from the government to introduce *waqf*". The inclusion of *waqf* in the Ninth Malaysia Plan is a clear example of this.

Thirdly, for *waqf* financing federal government public expenditures to take place, the issues addressed in this thesis must be tackled accordingly. This means that it takes longer time for federal government debt to be reduced which was similarly stated by Academician D. Despite this fact, the thesis itself has offered practical solutions to these issues as was discussed extensively in Chapter 6. By knowing the solutions, the time-period for successful implementation should logically become shorter. Furthermore, this thesis had provided the modus operandi for *waqf* financing pure and mixed public goods which ultimately depends on the decision of relevant authorities on whether to implement it or not.

Fourthly, one may argue that the use of parameter values sourced from the literature instead of estimating using current data can lead to questionable findings. However, this researcher believes that obtaining parameter values from the literature are more accurate as the cited studies had focused specifically on determining said values. Moreover, data on *waqf* value is lacking for an accurate estimation to be done. Besides, supplying from the literature helps mitigate the long time span for this research process. To ensure that the results are robust, parameter values that differ from baseline values were also incorporated. Despite all these constraints, the qualitative result had supported the quantitative result whereby federal government debt was able to reduce, hence, the findings of RO 3 and RQ 4 is still valid.

Fifthly, the appointment of YWM as the trustee of philanthropic *waqf* (*waqf* for public expenditure) may in reality, be impractical in light of the Malaysian legal framework of *waqf*. This is evident in Sharifah Zubaidah (2016) whereby the attempt to instate Federal Territories *Waqf* Act did not materialise due to sensitivities regarding the State Laws and the jurisdiction of Rulers within each state. In defence of this limitation, this thesis had also suggested that SIRCs may remain as the trustee of private *waqf* and religious *waqf*.

In other words, the mentioned sensitivities were taken into account to some extent. As opposed to Sharifah Zubaidah (2016), the Federal Territories *Waqf* Act requires that all categories of *waqf* be streamlined.

Sixthly, this thesis had not gone into depth on how the political economy of current majority Muslim states had evolved from past Muslim states; thus also reforming the relationships of state-private and state-individual relationships. In turn, these relationships affect how *waqf* would interact within the current political economic state. Hence by research standards, the forming of Figure 2.8 might be viewed as not having a strong basis. Regardless, Figure 2.8 had argued the place of public *waqf* specifically within Malaysia based on the country's *waqf* landscape. The country's *waqf* landscape had been extensively reviewed in Section 2.4 and had shown that the federal government had also endowed *waqf irsod*. *Waqf irsod* is sourced from the federal government budget hence making *waqf* a component of public finance too.

8.4   Research Implications

Albeit certain limitations, this research has a number of significant implications. For one, this thesis had successfully identified Malaysian *waqf* issues and provided realistic improvements on that issues, thus, adding further knowledge to the existing literature. Even more so, this study had determined the suitability of using *waqf* to finance certain federal government expenditures through arguments given by interviewees and the proposed model illustrated in Figure 6.4.

In addition, this research had shown that *waqf* financing public goods and social services can indeed help mitigate the Malaysian federal government debt problem without compromising welfare. This could happen in two ways. First, as *waqf* is now financing

public goods and social services, idle taxes can then be channelled to finance federal government debt. Second, the federal government would not need to borrow a large sum in the future as internal financing from *waqf* has been acquired.

On top of that, this study had revived the function of *waqf* financing public goods and social services in modern economy by introducing (1) a *waqf* framework (Figure 2.8) and, (2) a model for *waqf* financing these expenditures (Figure 6.4). The *waqf* framework is especially important in determining the place of *waqf* in modern economy. It is hoped that this framework can produce other studies of *waqf* in the modern economic setting. Meanwhile, the model for *waqf* financing public expenditure can become a point of reference for the relevant authorities to implement *waqf* in such a way.

Furthermore, this research has expounded the role of *waqf* outside of its typical religious purposes. It provided evidence to the claim that *waqf* is a versatile instrument to which it can adapt to changing economic environment while retaining its principles. Last but not least, this thesis had provided evidence that Islamic economy and the third sector can be part of the modern economy. Most studies had forgotten in all its gusto that household, which is an economic agent, consist of human beings that have feelings, values, and a moral compass. Thus, this thesis had helped to rediscover a missing component in modern economics which is altruism.

8.5   Suggestion for Further Research

There are a host of ideas that can be suggested to further this research due to the major exploratory nature of this thesis. First, a study can be done to determine the level of altruistic behaviour in Malaysians. Interested researcher can design a set of questionnaires and distribute it all over the country. It is possible to be done at such a large scale because

questionnaires can be distributed online. The questionnaires should also be designed as short as possible to attract respondents. Produced result, if positive, may well further support the findings from this thesis. Second, another study should also be done on the perception of *waqf* by the general public. How does the general public view *waqf*? Does the general public know the role of *waqf* in economics and finance or they view it from the lens of religion only? What is the best way to educate the public on *waqf*? These are all important RQs.

Third, a research should be done to determine whether the inevitable loss from *waqf* investment, after exerting all resources of the human intellect to manage risk, can be compared to the destruction of *waqf* properties due to natural disaster. It is the belief of this researcher that inevitable loss in *waqf* investment is the widest gap in the *Shari'ah* literature of *waqf*. Fourth, studies should be conducted on how to address the inalienability principle of *waqf* so as to make *waqf* trading in the capital market possible. As was mentioned earlier in this thesis, SC is prepared to regulate the capital market for *waqf* should issues like this be resolved. Interested researchers can employ the opinion of the Maliki madhab that allows temporary *waqf* and support the structure of said *waqf* using Islamic financial contract.

Fifth, Islamic Finance researchers can perform a study on the best investment portfolio for *waqf*. A thorough assessment on risk and return of Islamic financial equities and securities offered in the capital market can inject confidence for *waqf* managers to invest. This portfolio of investment can then be converted to a *waqf* unit trust. In fact, the said study can become a reference for *waqf* managers. Lastly, interested researchers can quantitatively examine other impact that *waqf* might have on the economy such as economic growth, wage rate, unemployment, and others. This researcher is optimistic that

the total value of Malaysian cash *waqf* will be made transparent in the future. Therefore, future researchers may as well model cash *waqf* collection using the AR(1) process.

8.6   Conclusion

A cohesive interpretation of the qualitative and quantitative strands provided a strong foundation for the future practical application of *waqf* financing public expenditures. Issues that may arise had been addressed and a model for the mobilisation of this idea were developed. The very fact that *waqf* financing public expenditure addresses the problem statement suggests the novelty of this thesis. To be clear, *waqf* financing public expenditure can reduce debt and primary deficit, as well as offer an alternative to the mix strategy of increase in tax and decrease in expenditure. Despite a few limitations, there are also significant research implications. The research provided a futuristic view on the issues that may arise from *waqf* financing public expenditures and how to address them. It brings to light the economic side of *waqf* and showed how *waqf* as a third sector component can contribute to modern economics. The contribution showed in this thesis are *waqf* financing federal government expenditure and the decrease of federal government debt. Perhaps, the suggestions for further research can be seen as a research implication too. This is because more research would boost confidence in said *waqf* application which could eventually put the idea into practice.

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