

The Nexus of Islamic Finance and Halal Industry: Bridging A Gap in Halal Economy

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ABSTRACT :

Islamic finance and Halal industries are part of Halal economy. Both industries are robust and thriving locally and globally. The great impact of Halal industries globally is celebrated because it is seen as companion to the Islamic Finance that already established long ago. However, both industries are lacking of nexus. This paper reviewing the selected literatures within the same theme. The finding shows that the integration between the industries is minimal due to lack of penetration which contributed by the lack of awareness among public and businesses to use Islamic financing as their capital to Halal production. This paper tries to describe briefly the scenario and the future outlook to integrate between both industries.

Keywords:

Islamic Finance, Halal industries, Halal economy

1. INTRODUCTION

Halal economy is a new term which might not necessarily exact similar as Islamic economy. While Islamic economy deals with wants and scarcity and its extension to Islamic concept, Halal economy comprised of almost every sectors (Mohd Ali, 2014). Malaysia International Islamic Financial Centre has divided the global Halal economy into four (4) main sectors as follows:

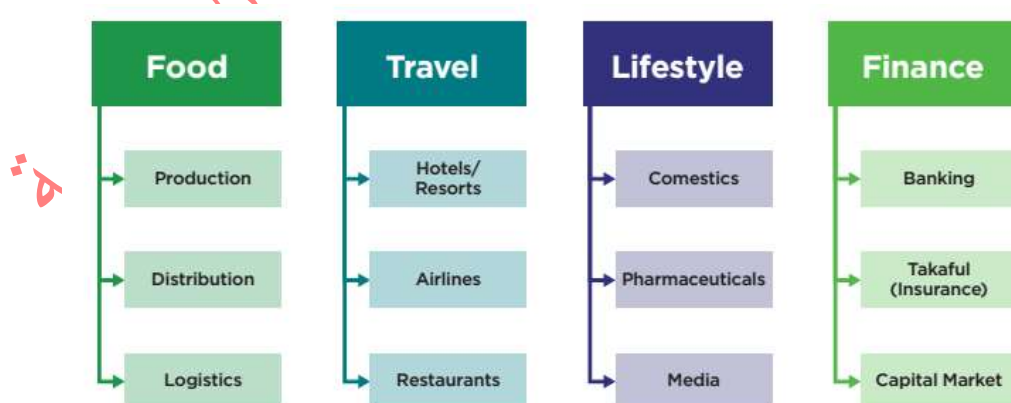


Figure 1: Global Halal Products and Services Ecosystem
(Source: MIFC (2014), pg. 2)

The term of Halal economy has been discussed by Irfan Ishak & Che Man (2011), Irfan Ishak, M. Daud, & Suhaimi (2014), Mohd Ali (2014) and MIFC (2014). Halal economy is the combination of Islamic finance and Halal industries. This is because the values and the principles lies within the industries are similar. i.e. based from Holy Quran, *Ahadeeth* (Sayings of the Prophet Muhammad PBUH), *Ijma'* (Consensus of Muslim scholars), *Qiyas* (Analogy) and *Ijtihad* (Logical reasoning). It means, the Islamic finance and Halal industries are inter-related and a perfect symbiosis nexus. However, the current scenario looks like both main industries are somehow separated and independent (Irfan Ishak, et al., 2013; Mariatul Aida & Rosidah, 2013; Mariatul Aida & Rosidah, 2014; Nurul Aini, Nathasa, Sumaiyah & Nor Asiah, 2014; Purnomo, Rosidah & Faridah, 2015). Thus, this paper tries to describe briefly the phenomena and the future outlook to integrate Islamic finance and Halal industries to strengthen the Halal economy.

2. METHODOLOGY

This is a general review paper. This study will apply the content analysis as a methodology. Content analysis is a process of synthesizing which play a vital role in knowledge dissemination and to give a further outlook of future research, policy, practices and public perception. Descriptive content analysis is a systematic review, that aims to identify the general trends and research results (Çalik & Sözbilir, 2014). This study uses this method because the integration of Islamic finance and Halal industries is empirically and conceptually in infancy locally and globally, although both industries have gone a long way to make an impact to the global world. It also intends to give a glimpse on the integration and interdependence of both industries. The secondary sources are used for this study for example the journal articles, proceedings, online reports, and other relevant documents.

3. LITERATURE REVIEW

3.1 Principles in Islamic Finance and Halal Industries

Islamic finance is a business transaction that based on the doctrines Shariah which the main philosophy is the prohibition of *riba'* (usury).

In Islam, the trade is permissible but *riba'* (usury) is prohibited. Allah said in Holy Quran, "Those who devour *riba'* (usury) will not stand except as one whom the devil has driven to madness by his touch stands. That is because they say trade is like *riba'* (usury), but Allah has permitted trade and forbidden *riba'* (usury)." (Al-Baqarah 2: 275). In other verse, Allah said, "Allah blights *riba'* (usury) but blesses charitable deeds with multiple increase." (Al-Baqarah 2: 276). Allah also warns the Muslim on the prohibition of *riba'* as stated; "O you who believe, fear Allah and give up what remains of *riba'* (usury), if you do not, then warned of war from Allah and His Apostle" (Al-Baqarah 2: 278-279).

Ibn Mas'ud narrated, "'The Messenger of Allah (ﷺ) cursed the one who consumed *riba'*, and the one who charged it, those who witnessed it, and the one who recorded it." He said: There are narrations on this topic from 'Umar, 'Ali, Jabir [and Abu Juhafah]. The Hadith of 'Abdullah (bin Mas'ud) is a Hasan Sahih Hadith. (Reported from Jami' al-Tirmidhi, Book 14, Hadith no.3).

Warde (2000) has stated that other than *riba'* (usury) prohibition, Islamic finance also prohibit *gharar* (risk, uncertainty and speculation) and the activities and transaction must be Halal, promoting justice, aiming ethical and religious goals, in order to attain *falah* (success) in this world and hereafter.

Halal industries are operating under the same doctrine. Allah stated, “O ye who believe! Eat of the good things that We have provided for you, and be grateful to God, if it is Him you worship.” (Al- Baqarah 2: 172). In another verse Allah said, O ye people! Eat of what is on earth, lawful and good, and do not follow the footsteps of the evil one, for he is to you an avowed enemy.” (Al-Baqarah 2: 168). This verse has been interpreted by Imam al-Qurtubi, stating that something is not Halal unless with the knowledge and non-Halal is any property which are *riba'*, sacred, *suht* (bad, fraud, contempt and *syubhah* (dubious) (Irfan Ishak & Che Man, 2011).

There is also a hadith on the importance of Halal in consumption and *riba'* (usury) avoidance. Narrated by Ibn Mawardaih, Ibn Abbas said: Al Baqarah verses 168-169) were read to Saad bin Abi Waqqas, “O Messenger of Allah, how can God allow my prayer?” “The Prophet said, “Look for good food then your prayer will be allowed, indeed a man who swallowed an illegal gratification in his stomach, then his prayer will not be accepted for 40 days, that a slave who grows meat from *suht* (forbidden food) and usury, the fire was most important to him” (Reported by Ibn Abbas) (Irfan Ishak & Che Man, 2011; Irfan Ishak et al., 2013). This hadith indicate that the prayer of a Muslim will not be accepted with the consumption of non-Halal food and the takings of *riba'* (usury). This shows that Muslims must preserve their consumption in both aspects, which makes them are closely related.

3.2 The Market of Islamic Finance and Halal Industries

Both Islamic finance and Halal industries are currently in great demand. This is due to the population factor, which sees the growth of Muslim populations around the world. The demand for Islamic finance and Halal products and services also accelerated by the emergence of Internet, early reception of Islamic teaching, obtain of higher educations and higher disposable income (Abdullah Swidi et al., 2010).



Source: Adapted from Fleishman-Hillard Mujlis, The Next Billion: The Market Opportunity of the Muslim World, ISRA

Figure 3.1: Muslim Population and Estimation of Growth in 2030 and 2050
Source: MIFC (2015), pg.1

Islamic finance has grows tremendously. It has begun a long way its components are currently in attention as an alternative of conventional finance to cope with the financial and economic downturn. Islamic finance comprises of Islamic banking and finance, Islamic capital market (Islamic funds), *Sukuk* (Islamic bonds), *Takaful* (Islamic insurance) and retakaful, Islamic microfinance, and other products. In 2014, the estimation of the total assets of Islamic finance is approximately USD 1.8 trillion and will projected to achieve USD 3.25 trillion in the year 2020. The following figure shows the market segments of the Islamic finance.

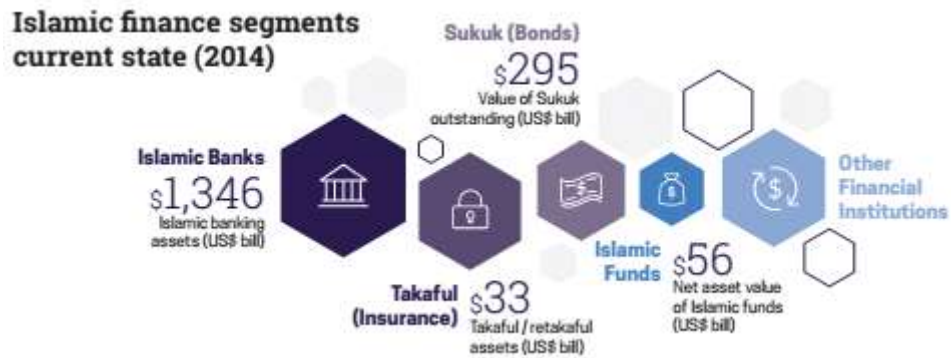


Figure 3.2: Islamic Finance Segments Current State (2014)
 Source: Thomson Reuters & Dinar Standards (2015), pg. 41

Halal industries, as mentioned earlier comprised of food, lifestyle and travel industries. This for example include the food products, processed food, meat, beverages, restaurants, abattoir, cosmetics, pharmaceuticals, media, fashion, logistic, hospitality and tourism. The Halal industries is the lucrative businesses and becomes a trend and lifestyle of consumers because its wholesome concept. The industries have created a greater demand and most of Muslim countries are competing in making a global impact of their presence in the industry. This also with the purpose of creating a global and international trading and create a hub of their niche Halal products which they have the competitive advantage, as been performed by non-Muslim countries for example Australia and India for Halal meat. The following shows the global Halal economy by sectors for 2012 and the forecasting of the market for the year 2018, which indicate the huge potential, market and demand.

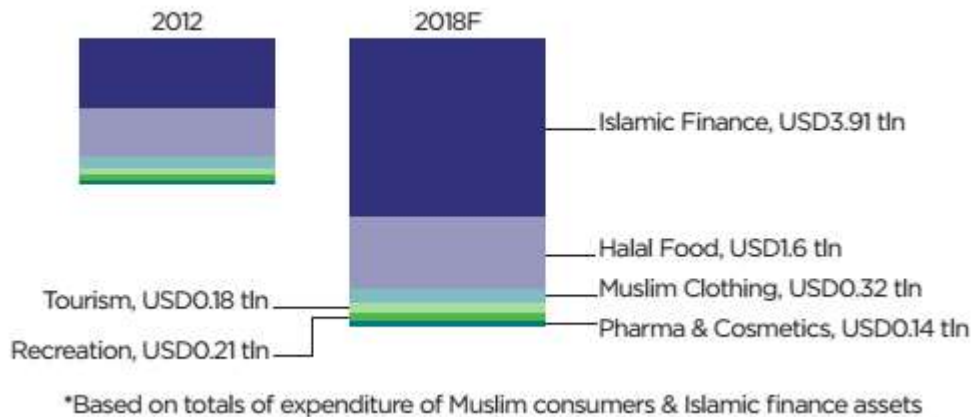


Figure 3.3: Global Halal Economy by Sectors (2012 and 2018F)
 Source: MIFC (2014), pg. 5

Malaysia is recognized as a leader in both industries; Islamic finance and Halal industries. According to the report by Thomson Reuters & Dinar Standards (2015), Malaysia have a comprehensive Halal economy ecosystem, with its thriving development of management system in both industries. It also considered as pioneer and champion in four (4) Halal economy components; Islamic finance, Halal food, Halal travel and Halal cosmetics and pharmaceuticals. This recognition is based on certain criteria such as the market size, demand/supply drivers, governance, awareness and social consideration (Thomson Reuters & Dinar Standards, 2015).

3.3 Related Studies

Currently, there are limited studies on the integration of Islamic finance and Halal industry, conceptually or empirically. As mentioned before, both industries although positioned under Halal economy with the same principles and value, somehow seems lack of nexus. Most of the studies were conducted in the realms of consumer behaviour, producer perception and practitioners' experiences in both industries but not crossing the paths of both industries.

Mariatul Aida & Rosidah (2013) has stated that it happened due to low penetration of Islamic finance among Halal industry players. MIFC (2015) also mentioned the same thing; that this low penetration is mainly due to low awareness and perception of Islamic finance and Islamic capital market by consumers and investors. Mohd Ali (2014) reckons it happened because the Halal product producers are mostly dominating by non-Muslim producers hence the utilization of Islamic finance is not maximized. Furthermore, there is no linkage in the method of financing to the Halal compliance. In other words, there is no requirement of the Halal product to be financed by Islamic financing, although in Malaysia there is a very strict requirement in other aspects of production (Nurul Aini et al., 2014). In Malaysia, as in the year 2008, less than 10 per cent of the Halal product producer use Islamic financing as their source of capital (Mohd Ali, 2014).

Mariatul Aida & Rosidah (2013; 2014) has built a framework which used TPB (Theory of Planned Behavior) in measuring the attitudes of the SMEs (Small Medium Enterprise) to use Islamic financing, with five (5) independent variables; (i) awareness and knowledge (ii) religion obligation (iii) cost benefit (iv) business support and (v) reputation. In their preliminary studies to 30 SMEs the findings has shown that only 40 percent of the SMEs are currently using the Islamic finance while 50 per cent never used one. The half of the SMEs also to be found have limited knowledge to zero knowledge of Islamic financing (Mariatul Aida & Rosidah, 2014).

Purnomo et al., (2015) has proposed an Integrative Model of Behavioural Prediction in the studies of the intention and behaviour prediction of Halal food and services businesses and firms. It is the extension of the studies by Mariatul Aida & Rosidah (2014), which they adding up other independent variables; (vi) Halal literacy and (vii) customer service quality.

Nurul Aini et al., (2014) has opined that there are still rooms for adjustment of integration between Islamic finance and Halal industries. The studies trying to look the regulations and governance of the Malaysian authorities in Islamic finance and Halal industries. Three governing regulations has been compared which are (i) Halal product manual procedure by JAKIM (Department of Islamic Development of Malaysia) (ii) Shariah-based Quality Management System by DSM (Department of Standards Malaysia) and (iii) Screening methodology by SC (Security Commission of Malaysia) for Islamic capital market. The studies found that there is a leniency in terms of financing for Halal product, in contrast with Islamic capital which needs to be Islamic financed to be considered as Shariah compliant.

Irfan Ishak et al., (2013) trying to merge of both industries in three main areas; (i) research and training (ii) law, regulation and standards and (iii) promotion and development. It is found that for regulation and promotion both industries have different bodies and authorities in governing the industries, but similarities found in the area of research and training. The tools for Islamic finance toward the Halal production have been elaborated by Syahida & Siti Syafira (2015). Among the tools of Islamic finance are Mudharabah (silent-partnership enterprise), Musyarakah (partnership) which has been described extensively.

4. FUTURE OUTLOOK

4.1 Nexus of Islamic Finance and Halal Industries

Halal economy is relatively new compared to Islamic economy. To ensure the component Halal economy is integrated to each other, the linkages of the industries must be well connected. The Islamic finance and Halal industries should not be treated singularly, because basically they have been mentioned solidly in Holy Quran and *Ahadith* simultaneously. Additionally, both have the same principles and values. The businesses and firms should use Islamic financing to raise their capital, to ensure the whole supply chain is Shariah compliant. MIFC (2014) has shown the mutual relationship of Halal industries and Islamic finance, which both can gain wider access of funding and penetration and also bigger market share.



Figure 4.1: Nexus of Islamic Finance and Halal Industries
Source: MIFC (2014), pg. 7

4.2 Harmonization of Governance

As mentioned previously, Irfan Ishak et al., (2013) and Nurul Aini et al., (2014) has provide the attempt of the synchronization of the Islamic finance and Halal industries' governance system. The governance here consists the regulation, authorities involved, compliance requirement and Shariah review and audit.

In the case of Malaysia, Halal industries is bound by the Halal Standards by DSM (Department of Standards Malaysia) and JAKIM and Halal Assurance System Management 2013 (HAMS 2013) for the review and auditing purposes to ensure the transparency and credibility of Halal product. Zurina & Siti Noradibah (2015) has proposed the integration of Shariah Governance Framework 2010 (SGF 2010) which is implemented in year 2011 by Bank Negara Malaysia (Central Bank of Malaysia) for Islamic finance institutions into the HAMS 2013. The SGF 2013 is considered as complete guidelines for Shariah review and governance (Zurina & Noradibah, 2015), while HAMS 2013 only provide the basic guidelines and reviewed periodically or the occurrence of non-conformities. i.e. non-compliance. It is understandable because HAMS 2013 is relatively very new and in infancy stage. Thus, it is hoped that HAMS 2013 can be improved, at least to achieve SGF 2010 to ensure the Shariah compliance reviewing and monitoring process of the Halal product.

Nawal, Sheila, & Syed Ahmad (2013b) has proposed on the internal Shariah review in Shariah compliant companies for Islamic capital market. This is because the screening methodology by Security Commission of Malaysia (SC) for Shariah compliant companies is involving only external review hence they proposed the internal Shariah review in the Islamic capital market. The SGF 2010 is used as a benchmark. Nawal, Sheila & Syed Ahmad (2013a) opined that the standard of Shariah governance guidelines is too general. The Shariah governance definition in AAOFII and standards by Bank Negara is lack in solid definition, compared to IFSB definition (Nawal, Sheila & Syed Ahmad, 2013b). They also propose on integrating conventional corporate governance to the Islamic capital market for monitoring purposes.

4.3. A Way Forward

Based from the literature review, we found that the lack of nexus between Islamic finance and Halal industries is due to lack of awareness and knowledge among public and businesses. The perception also play a role, which make the businesses thoughts the Islamic financing is way more expensive compared to conventional financing (Mohd Ali, 2014). Islamic financial literacy and Halal literacy must be promoted through the channels available to promote awareness among public and businesses. The channels may be in forms of existing training provided by both industries and the promotion/campaign by the regulators. Regulators and training providers must promote the advantages of Islamic financing and the production of Halal product and services so that the public can distinguish the difference of conventional financing and Islamic financing. This can encourage more businesses to use Islamic financing and producing Halal products and services to strengthen Halal economy. The syllabus of their training should include and harmonize the components in Halal economy so that businesses and practitioners not treat the industries separately.

Islamic finance and Halal literacy should not only be promoted to Muslim producer, but also to non-Muslim business owner. The Halal concept literacy has been successfully accepted by non-Muslim consumer due to its wholesome concept and environmental-friendly business (Zurina & Wan Siti Khadijah, 2012; Rezai, Zainalabidin & Mad Nasir, 2012). Not only for Halal food, but the awareness level has reaching the non-food Halal product, and thus Malaysia has been one of the top countries in the market of non-food Halal products like cosmetics and pharmaceuticals (Rahim, Shafii & Shahwan, 2013). Thus, the awareness introduction of the Islamic finance to the non-Muslim business owners is not impossible.

The regulators or government also play a role in the integration. It will be a good move if the government or regulators can waive for Halal certification fees or other fees if the businesses uses Islamic financing. This may promote awareness of the firms or producer to use the Islamic finance product. Government or regulators also may introduces a special package for young entrepreneur of SMEs that want to venture into Halal product, which the package in like 2-in-1; use Islamic finance product for capital and Halal certification for their product. Government or regulators may waive the administration cost or other fees in the initiation of the businesses, thus gearing up the Halal economy.

The Halal economy also needs the human capitals that are well-versed in both industries. Thus, the discussions of the Halal economy will be inter-connected, seeing in both angles and consequently gaining the public confidence.

Future research may involve the confidence of the businesses and producers to the Islamic finance system. Most of the time, the public perceive Islamic finance have the similar mechanism with conventional finance; exclude the elements of *riba*' (usury) and *gharar* (speculation). However, Islamic finance have a special mechanism to comply with Shariah, to protect the credibility of the transaction and to build a good rapport among the people involve

and to preserve the good reputation. The mechanism of Islamic finance, although perceived as similar with conventional finance, is actually an alternative to get the transparent funding and capital. This actually encompassed the matter of our submission to Islam, our belief as a Muslim, to attain the blessings from Allah, in this world and the hereafter.

6. CONCLUSION

Islamic finance and Halal industries are both robust locally and globally. Both are the huge part of Halal economy system as described by MIFC (2014) and Irfan Ishak et al., (2014). However, the findings show the disintegration between those two. This is due to lack of penetration among them, and lack of awareness among public and businesses. There are some of the proposals on the integration which mostly begin with governance system. This paper tries to incorporate both in every level; government or regulator, businesses, and public. This is to strengthen the Halal economy and to boost of industries to the next level.

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