THE ROLE OF ISLAMIC FINANCE IN THE COVID-19 PANDEMIC

Prof. Dr. Shamsher Mohamed Ramadili Mohd & Prof. Dr. Zulkarnain Mohd Sori
Leading the way in conscientious knowledge sharing, empowering enterprise and individuals to overcome uncertainties while contributing to a better world.

At INCEIF, we embrace innovations and resilience to move rapidly towards a successful recovery.

JAN 2021 INTAKE IS NOW OPEN

APPLY NOW

marketing@inceif.org  www.inceif.org
Editor’s Note
by Assoc. Prof. Dr. Baharom Abd Hamid

In Person:
COVID 19: The Role of Islamic Finance
by Prof. Dr. Shamsher Mohamed Ramadili Mohd & Prof. Dr. Zulkarnain Mohd Sori

From Industry’s Table:
Sukuk PRIHATIN: Malaysia’s First Digital Sukuk
by Puan Ruslena Ramli

From Faculty’s Table:
Blended Islamic Social Finance – Micro Takaful Model: Protection and Provision for Pandemic Crisis
by Dr. Shinaj Valangattil Shamsudheen

From Faculty’s Table:
Pandemic Innovation for Zakat: The Potential of Crypto Zakat
by Assoc. Prof. Dr. Aishath Muneeza

INCEIF’s Alumni:
My Journey in Islamic Fintech
by Mr. Mehdi Baddou
Assalamualaikum wbt,

Alhamdulillah! Praises to Allah, for all the blessings that He has bestowed. Despite the conditional movement control order (CMCO), we managed to produce the 4th issue of IF HUB for 2020. The unprecedented pandemic has redefined the workplace norms across industries, including Islamic finance.

In this issue, we are honoured to have Prof Dr Shamsher Mohammad together with Prof Dr Zulkarnain, wrote on the Role of Islamic Finance Post Pandemic. The article discussed on the important role of both the Islamic finance sector and the government to develop a new sustainable culture to work closely with the private sector while striking the balance between short and long-term measures. We are also privileged to have an article contributed by Ms Ruslena Ramli from RAM Rating. The article titled Sukuk Prihatin: Malaysia’ First Digital Sukuk, agreed that a durable economic recovery rest upon the collective effort between the government and private sector entities in addressing the current challenges which bring Malaysia as one stronger, more resilient and competitive nation.

From Faculty’s Table, we are pleased to have our respectful faculty members to contribute in this final edition of 2020. The article titled Micro Takaful Model: Protection and Provision for Pandemic Crisis, written by Dr Shinaj, was mainly discussed about the Islamic social finance instruments which could be essential in developing a micro-takaful model that can provide prime concern for the socio economic welfare during pandemic crisis. Dr Aishath Muneeza wrote an interesting article titled Pandemic Innovation for Zakat: the Potential of Crypto Zakat. This article deliberated well on the potential of crypto zakat which could enhance the transparency and integrity within collection and distribution of zakat. We are blessed to have our Alumni, Mr Mehdi, contributed to the final edition for year 2020. In 2016, after he graduated in MSc Islamic Finance (INCEIF), Mr Mehdi embarked on his journey in Islamic Fintech Industry. He shared his exciting experiences throughout his journey in his article. It is hope that the articles showcased in this final edition would benefit our beloved readers.

Last but not least my gratitude for all the players who have played key roles in making this special issue of IF HUB a reality, both directly and indirectly. We would also like to thank the readers for the feedback provided.

Feedbacks and comments are most welcome.

Assoc. Prof. Dr. Baharom Abdul Hamid
baharom@inceif.org
INTRODUCTION

COVID-19 pandemic is a virus-related natural disaster. The Covid-19 pandemic was detected in 2019 in Wuhan in China and then spread to Hong Kong and then other countries, as it has considerably broader reach in terms of numbers of both countries and people affected than other virus-related disasters (Hassan et al. 2020). The possible reason for this global contagion is the increased integration of the global social and economic supply chain linkages so entrenched in the globalized ecosystem since 1980s. These previous virus-related pandemics including Severe Acute Respiratory Syndrome (SARS) (2002-03), Swine Flu (2009-10), Middle East Respiratory Syndrome (MERS) (2012-13), Ebola (2014-15), and Zika (2016) had a relatively high mortality but low infection rates compared to Covid-19 that is highly contagious but relatively less fatal but generating greater economic losses due to its prolonged persistence (Verikios et al., 2011).
The prolonged nature of this pandemic has halted the global economy and caused substantial socio-economic adversities in all economies, albeit more in emerging and developing economies that have greater vulnerabilities of poor population, lack of financial resources and infrastructure to provide reasonable health services in normal times, let alone during pandemics. Covid-19 have beaten them all by affecting the economy and financial systems of almost 211 countries, with more than 50 million diagnosed and 1.2 million deaths at the point of writing this article (November 2020). This pandemic has contributed to mass economic destruction due to total and partial lockdowns of the economy, economic disruption through reduction of output or even closure of factories and increase in unemployment. Since the pandemic is global, the export-oriented economies suffer greatly as importing countries reduce their imports due to decrease in demand for goods and services.

With the global economy under lockdown, governments are pursuing emergency fiscal measures to mitigate the short-term effects of drastic interruptions to the normal income, credit, and spending patterns among businesses and households. Though these measures are politically expedient, the real effectiveness of these measures depends very much on the extent of pre-existing vulnerabilities such as the levels of leverage, the dependence on large external financing needs, and the level of existing political, social, economic and financial structural issues (Huidrom et al. 2019). In heavily populated countries like Indonesia and India with absence of any social support system, the general workers are willing to take the risk to work in vulnerable environments and impedes the containment measures to stop the spread of the virus (Corburn et al. 2020; Farzanegan, Feizi, and Gholipour 2020; McKibbin and Sidorenko 2006). This leads to fast spread of the virus and greater social costs of treatments and fatalities. For governments, there is a trade-off of either taking effective measures to control the contagion through various measures or spend more resources on treating those affected with their limited facilities and resources.

It is almost a year for the Covid-19 pandemic with more than 161 centres working on the potential vaccine with varying degree of self-proclaimed success. The latest is the vaccine developed at the Oxford University in the UK with 70% of success in helping individuals not getting infected, but nothing with regard to curing those who are already affected. On the other hand, Pfizer reported a 95% successful rate in protecting from COVID 19. As a result, the Malaysian government has signed a purchase agreement to immunise 20% or 6.4 million of the population with a condition that the vaccine must be registered with the US Food and Drug Administration (FDA) and Malaysia’s National Pharmaceutical Regulatory Agency (NPRA).

**ROLE OF ISLAMIC FINANCE**

Islamic finance is a financial system that creates, preserves and distributes wealth based on ethical and moral principles that do no injustice to anyone of the stakeholders. The value proposition is that it is social centric, ensures justice for all, ethical and upholds morality for all God’s creation. These principals become more relevant in times of pandemic when the economic and social systems are in chaos, that requires the system to walk the talk in mitigating the adversities of the pandemic on the populace.
Malaysia, is a good setting for testing the role of Islamic finance in the pandemic, as it’s population is predominantly Muslims and is currently a global Islamic Finance hub. To date, nothing much has been apparent, except for government handouts to ease the burden of the great majority of the poor sector of the population. This brief suggests some unique initiatives that Islamic Finance could afford to substantiate the government’s initiatives to lessen the burden of the populace and hopefully ride-out of this pandemic and get the economy and livelihood normalized again.

First, it must be noted that irrespective of Islamic or conventional, there is a dire need for the private sector (financial or otherwise) to support the government’s initiatives to protect jobs. Since the crisis began in March 2020, more than half a million workers have lost their jobs. Currently, SOCSO has taken the initiative to provide subsidy scheme for employer to retain their employees. This is a good stop-gap measure to buy time to ride out of the pandemic. If firms have high operating leverage and operations costs with less revenue inflow, they will not be able to retain their workers. Probably, the subsidy scheme with reduced working days for the workers could help reduce the unemployment figures and keep the demand for goods and services rolling, albeit at a low level. Islamic financial sector should emulate this noble initiative for their institutions as well. The Islamic finance sector could bear most of their payroll costs and retain their workers. After all, they can use the Zakat funds and the Penalty funds (Gharamah) in these institutions, besides the tax incentive packages from the government.

Islamic finance can play a critical role by funding the social, health and education programs. In the societal programs, there could be more funds allocated to technological innovations and more important to support micro and small business financing for those who are willing to venture and make a small livelihood for themselves. They should provide free capital and advisory service to those qualified for this scheme and for those who have lost their small businesses due to lack of working capital. Islamic banks could provide this financing in the form of Qard financing with no interest or even Qard Hassan financing with no requirement to payback the capital borrowed to micro businesses to help people start financing their livelihood.
For long term planning to face future pandemics and crisis, the lesson from current experience is that there should be some kind of periodical savings in each business’s institution, besides the zakat funds which are obligatory, and to be invested with effective governance. When there happens to be a crisis, these funds will then be used to help retain workers and help the society-based programs. This is modelled on the citizen-funds concept currently in practice by Norway and other developing countries. The government made it compulsory for businesses to contribute to this fund that is invested and governed by the government, and can only be utilized in times of crisis or pandemics. On the national scale, the government could do the same, for example, when the economy recovers, a percentage of wealth created by the joint government and private sector, wealthy individuals that work on government projects and all government-linked firms make periodical contribute into a national crisis fund. These contributions can be treated as tax-deductible expenses to incentivize these contributors, similar to the spirit of public fund created by the previous government to help them pay-off government debts. The proceeds of this fund can only be used for national emergencies only and invested diligently with proper transparency and governance, and the progress of the fund be tabled in the parliament annually.

Another long-term initiative could be for the government to start infrastructure projects (like highways, stadiums, hospitals, schools etc) both at state and federal level to create employment and restart the economy. Islamic finance institutions could come together and issue Sukuks to support these projects as their long-term investments. We had successful experience of this strategy after the 1997 and 2007 crisis using proceeds from bond issues and whatever development budget there was to enabled us avoid begging for IMF funds, and managed to recover the economy, albeit at a slower rate than expected.

For the educational sector, the pandemic has necessitated closure of both private and public educational institutions for a prolonged period, and forcing the delivery where ever possible through on-line mode. This requires a well set-up internet infrastructure to facilitate the smooth operation of online classes. Unfortunately, not all areas or families have access to the required internet services and this has caused a lot of students to drop-out of the education programs usually conducted in normal times. This is an area where government should not only relieve parents from the fees and other expenses usually charged for the educational facilities but get the internet companies to collaborate with the Islamic finance institutions to provide the internet services where it is needed using their zakat and penalty funds, or even provide these facilities in areas without the internet services, free of charge to affected students.

Another initiative to support the poor is to reactivate the agriculture sector which includes vegetables farming and breeding goats, cows, and chickens on a small-scale farming on idle lands in towns and villages. Affected needy families eligible for this project could work with local authority for using government lands (like river banks or land around railway tracks and high ways) and to mobilise relevant agencies like FAMA for distribution of products to be sold in day and night-markets. Participants should be provided with the capital from Islamic financial institutions and zakat authority, preferably in kind (like, seeds, fertilizer, pesticides, and technical advice) and do not have to pay back anything.
Another initiative to provide short-term relief to the hard-core poor sector of the population by creating Kitchen Soups all over the countries to provide at least two meals a day to these people, preferably through the cooperation of mosques, churches and other place of worships, and non-profit organizations. There should be an open fund to collect contributions to provide financing to food catering firms to revive their business and at time contribute to the society in times of need.

For those who still can afford to pay for their livelihood, provide them with heavily subsidized food items. Government should set up a company to buy main food items (like rice, flour, sugar, cooking oil, salt eggs etc) on a bulk scale from wholesalers and sell to the population at cheap prices. Another similar alternative is to buy the tin food items (like sardines, biscuits etc) that almost reaching their expiry date and distribute these items to the needy through proper channels to relieve their burden. Food items that are near expiry date could be bought from grocery stores in bulk at discounted prices and sell at a subsidized price to the public. This could address the buyer affordability issue as well provide some profits to the firms that provide this service.

**CONCLUSION**

The Islamic finance sector and the governments must develop a new sustainable culture to work closely with the private sector to not only initiate the short-term measures to support the needy, but need to think long-term measures to create jobs through infrastructural projects and developing Micro and Small-scale businesses.

The government on its part should reshape the economy through investments in acquiring technologies and developing technological skills and provide related education programs in the educational system.

The real trade-off for the government is the balance the choice between short and long-term measures. The short-term measures are politically expedient but are short on economic expediency for long term survival.

Whereas the long-term measures are economically expedient but are short of the political expediency much to the disliking of the ruling elite that are always focused on short-term dividends.

A strong political leadership and social trust are the necessary success factors for long-term survival and sustainability under the new-normal geo-political and reshaped globalized world.

**References:**


The Economist, October 10th, 2020


McKibbin, W., and A. Sidorenko. 2006. “Modeling Macroeconomic Consequences of Pandemic Influenza.” Centre for Applied Macroeconomic Analysis, Crawford School of Public Policy, Australian National University, Canberra.

Pursuing the financial inclusion agenda, has been among the Government of Malaysia’s (GOM) objectives listed in the Financial Sector Blueprint (2011-2020). Availing opportunities to all members of society to participate in the formal financial system remain a key component to Malaysia’s inclusive growth strategy. According to Bank Negara Malaysia’s (BNM) key indicators for financial inclusion - over a 10 year period the percentage of adults with at least one type of regulated deposit account and number of deposit accounts per 10,000 adults grew from 87% and 29,860 in 2011 to 96% and 30,640 in 2019. To date, Malaysia continues to record one of the highest increased in levels of financial inclusion among middle-income countries2.

Supported by these statistics, the GOM was able to put in place this innovative proposition fairly quickly (considering it took approximately six months) the country’s first digital sukuk. Access to individual’s deposit account facilitated the offering of Sukuk Prihatin, targeted to garner support from all Malaysians as the country battles the second wave of COVID-19.

It has been remarkable how, in times of adversities, the silver lining has been the people’s rally to become more socially conscious not just in aspects of public health and welfare, but also in supporting the local economy. Equally important is the participation from the private sector to also be responsible in re-energizing the economy.

Sukuk Prihatin was launched as a call for national solidarity to support the Government’s recovery effort and each other by funding targeted economic relief measures. Funds raised through Sukuk Prihatin will be used to enhance connectivity in rural schools, finance eligible micro enterprises (with a focus on women entrepreneurs) and research grants for infectious diseases. The sukuk carried a 2% annual profit payment, payable quarterly. Sukukholders have the option to donate part or all the principal amount when the sukuk matures in two years time i.e. 22 September 2022. As an incentive stimulus, all profits from Sukuk Prihatin are tax exempted and the principal sum donated is tax deductible.

Leading the sukuk offering was Maybank in their role as the Primary Distribution Bank. According to Maybank, the thought process that went into the structuring and operationalization of the sukuk issuance reviewed the best possible option which ticked the GOM’s agenda to support financial inclusion by bridging the digital divide through efficient connectivity.

Labelled as a social finance investment, the sukuk offering was performed digitally using BNM existing banking channels for transfers via JomPAY and DuitNow, accessible across twenty-seven banking platforms in Malaysia.

Launched on 18 August 2020, the Sukuk Prihatin’s offering period was made available for 1 month before it was closed on 17 September 2020. The initial RM500 million issuance size was oversubscribed, resulting in the final issuance amount to be upsized to RM666 million when it was issued on 22 September 2020. Some industry observers questioned the rationale the issuance not using Bursa Malaysia’s electronic trading platform which is readily available to enhance retail participation. That being said, not everyone have access to a central depository system account. The ease and speed of Sukuk Prihatin’s subscription process marks a turning point for future retail issuance to emulate and reach a far larger audience just by a mobile click away. Evidently, the GOM and the regulators’ concerted efforts in building a sustainable ecosystem to ensure delivery of financial products and services in a responsible and more cost-effective manner has made a positive impact.

---


4 The opening of a CDS account is a pre-requisite for investments listed in Malaysia stock exchange. Investors need to be 18 years old and a RM10 fee is charged for the CDS account opening. The CDS acts as a means of representing ownership and movement of securities. CDS account holders enjoy the convenience of obtaining electronic securities transfer and trade settlement.
Ultimately, a durable economic recovery rest upon the collective effort between the GOM and private sector’s shared prevalence to overcome current challenges and emerge a stronger, more resilient, and competitive nation.

The 133% over-subscription rate is a clear testament to the spirit of unity and solidarity among Malaysians in facing this unprecedented challenging period. As social finance is a core pillar of Maqasid Shariah – the Sukuk Prihatin marks another important milestone for Malaysia’s leadership in Islamic finance.
Globally, the COVID-19 outbreak disturbed all the segments of the population regardless the economic status of the country i.e. developed, developing and under-developed, and it was extremely harmful to the underprivileged segment (B40) of the societies in each country. The crucial measures implemented to contain the virus have triggered both economic and social depression. Significant weakening of economic conditions has escalated the tension on household, business units and financial markets. As shown in figure 1, degree of the vulnerability observed higher at the lower income households, and the adverse impact become significant within short span of time. Further, this pandemic crisis damaged all the basic necessities of the poor segment starting from health, food, job (according to the degree of exposure).
The deleterious consequences of COVID-19 indicate the unpreparedness of the economy to confront such pandemic, and it highly demands the protective measures to face such crisis in future. These measures should consider the socio-economic aspects (health, food, job, etc.) that predominantly exposed to the recent case of pandemic. One of the viable measures to take protective measures in order to prepare for the future crisis like pandemic is insurance/Takaful. The innate nature insurance facilitates both protective and development measures that can contribute to the wellness of the society and economy. The COVID-19 pandemic has amplified the significance of the insurance sectors’ role in health, social and economic resilience of individuals and businesses. Other than health issues, Lockdown measures have compelled many businesses not operating in essential services to temporarily close their doors. While this has a huge impact on all businesses, it is likely to hit micro-small-and medium-sized enterprises (MSMEs) the hardest. Without adequate reserves, appropriate insurance solutions or easy access to credit, many MSMEs are forced to lay off workers or worse, shut their doors permanently. This in turn has devastating effects on individuals’ welfare and economies at scale.

Micro insurance is one of the most appropriate tools that can play an important role in the global crisis such as pandemic since the micro-insurance provides a degree of protection for the world’s most low-income and vulnerable populations and those are the most affected population all over the world. The general concept of micro insurance is the same as one might use for regular insurance except for the clearly prescribed target market i.e. low-income people. The target population typically consists of persons ignored by mainstream commercial and social insurance schemes, as well as persons who have not previously had access to appropriate insurance products.
Micro-insurance can benefit a larger number of population as they make up the major portion of the total population in each country. Further, the small amount of contribution, current state of lower penetration rates in developing and developed countries are also additional factors that shows the potentiality of the micro insurance for these markets.

Although micro-finance has been successful in some of the developed countries, the success rate of micro insurance in developing countries is not remarkable. Some of the important reasons that can be highlighted for unsuccessfulness of the micro insurance in these regions are; a) inability of the people to make the payment of contribution during their financial difficult period; b) lack of support from the govt. and NGOs; c) Major focus of insurance providers towards profit making rather than social welfare. Further, what is lacking in the conventional micro insurance model is the attributes such as mutual assistance which is vital for the existence of healthy community or society. Islamic insurance or Takaful model is the one that operates with the philosophy and concepts of brotherhood and mutual assistance (ta’awun) and shared responsibility among members in providing financial aid and assistance to those who had incurred misfortunes, mishaps or faced difficulties. Takaful model operates based on the contract that is Tabarru’ (donation) where a participant agrees to donate a pre-determined percentage of his contribution (to a Takaful fund) to provide assistance of joint guarantee and mutual help should another participant suffer a loss. These special features of the takaful are critical where the socio-financial protection is essential to overcome the adverse effects of global crisis such as pandemic in which a collective cooperation is highly demanding.

Islamic social financial instruments have always been important consideration in Islamic financial services especially where the social consideration is involved. Islamic social finance tools have been instrumental in the alleviation of poverty and socio-economic development for many years. Some of the popular Islamic social finance instruments are Zakat, Waqf and Sadaqa (charity) which have been adopted and applied even outside the Islamic world. These instruments are employed to provide education and healthcare, develop infrastructure and maintain social welfare provisions for the poor and destitute. Hence, consideration of these Islamic social finance instruments is also essential in developing a micro-takaful model that provide prime concern for the socio-economic welfare and protection of society from the crisis like recent case of COVID-19.
Like other financial institutions, recent case of COVID-19 was relatively a new experience for the insurance/takaful sectors all around the globe. A large degree of confusions was evident in the insurance/takaful sectors in relation to structuring/providing coverage for their existing and new customers on pandemic crisis, and it explains the unpreparedness of the insurance/takaful institutions to address the crisis. While there is ample insurance/takaful plans accessible in the market that covers different sectors of the society (e.g. B40, M40, and T20) and serve different purpose for them (Health, Education, Life, etc.), insurance/takaful companies have not yet come with an insurance/takaful plan that consider the specifics of the pandemic vulnerability. A comprehensive and sustainable insurance/takaful business model that leverage the peculiar features of Islamic social finance instruments is highly demanding that provides protection for the individuals in the areas where the COVID-19 was adversely affected (e.g. health, food, job, education, financial stability, etc.). Hence, this report will illustrate a blended Islamic social finance-Micro Takaful Model that enables the protection and provision for pandemic vulnerabilities.

**BLENDED ISLAMIC SOCIAL FINANCE-MICRO TAKAFUL CONCEPTUAL FRAMEWORK:**

* Actuarial risk pricing will determine what can finally be covered for the beneficiaries
* Health protection (coverage) can be provided for both outpatient consulting and critical illness (to be determined)
* Role of IDB can be either contributor or manager or arranger of investment side of SMEs

---

**Figure 2**

* Actuarial risk pricing will determine what can finally be covered for the beneficiaries
* Health protection (coverage) can be provided for both outpatient consulting and critical illness (to be determined)
* Role of IDB can be either contributor or manager or arranger of investment side of SMEs
Figure 2 illustrates the conceptual framework of proposed micro-takaful business model in which the further research is required in order to validate the model. The model envelopes the important segments (i.e. underprivileged households (B40), employees in health sector, food security, job security/income stability) of the socio-economic system which are vulnerably exposed in the event of the pandemic. The proposed model offers an end to end business model in which the important aspects of takaful (protection (in the event of pandemic) and investment (for the business sustainability)) are ensured.

From the societal perspective, the proposed model confirms the provision for the health protection for underprivileged segments of the society and employees of the health sectors. Further, it also provides the means of food security and educational continuity in the event of crisis such as pandemic. From the economic perspective, the investment aspect of the model provides avenues for the MSMEs sectors (e.g. emergency care and agricultural) to be part of the system as income generator. It helps to empower and sustain the MSMEs sector to a great extent even during the crisis period (pandemic). Moreover, it also enables the job security and financial stability of the workforce of the society.

**BUSINESS MODEL**

The Waqf Micro-Takaful model is considered as the underlying business model. Generally, two types of cash inflows are taking place in the model i.e. in the form of takaful contribution and endowment fund. Takaful contribution is contributed by the insured/protected parties of the model i.e. underprivileged sector (B40) of the society and the employees in the health sector. Financial support from the Govt. can also be proposed in the form of partial payment of contribution for B40 segments. Endowment fund can be accepted in the form of waqf from the High net worth individuals and in the form of CSR fund of institutions. Hence, no monetary benefit is required to pay back. The underlying contract of waqf employed with respect to the accepting fund into the business model provides financial flexibility as there is no need to payback the return to the donors of the fund. and the returns can be either kept with the micro-takaful institution or can be reinvested.

Since the possibility of the materializing the crisis (pandemic) is relatively is less often, it is not economical to keep the fund received as idle, and it can be invested in appropriate sector.
As indicated in figure 1, some of the most exposed segments in the event of crisis are Health, Food, Employment. Hence, it is recommended to make the investment in these sectors (e.g. Personal Protective Equipment (P.P.E.) kits, urban and vertical farming, MSMEs). Investing in Health protection materials’ sector will enable to tackle the deficiency of necessary equipment such as P.P.E kits and mask in the event of pandemic crisis. Further, investment in modern farming methods such as Urban and Vertical farming and in emergency care materials production initiatives will enable self-sufficiency of food supply and ensure the availability of emergency care materials such as P.P.E kits and Masks for B40 segment, and it will reduce the dependency on external sources during the event of crisis such as pandemic. Likewise, investments in technology sector that develops the facility for education will help to facilitate means for pursue education for B40 sector even during the time of pandemic. The MSMEs sector plays a crucial role in the economy in generating revenue and providing employment. MSMEs sector accommodates a significant population B40 sector. As shown in Figure 1, it is the same sector significantly and negatively impacted by the recent COVID-19 pandemic. Hence, investing in MSMEs will provide the financial stability (by providing employment and entrepreneurial opportunity) to the B40 segment and empower the MSMEs sector of the economy. The MSMEs can be either existing (private or govt.) or newly established and managed by the subsidiaries of Takaful institutions. In the short term, the investment can be done in the existing MSMEs and dedicated MSMEs can be established in the long run.

**SCOPE AND FEATURES OF THE PROPOSED MODEL**

<table>
<thead>
<tr>
<th>Micro-Takaful Business Model Covering:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health Protection</td>
</tr>
<tr>
<td>Food security</td>
</tr>
<tr>
<td>Empowering MSMEs / Job security</td>
</tr>
</tbody>
</table>

**Table 1: Scope and Features of The Proposed Model**

- Potential wider Socio-Economic impact
- Viable and practical
- Replicable and scalable
- Patentable with commercial potential
- Sustainable
- Digitalization
- Greater inclusion

**CONCLUSION**

The illustrated conceptual framework need to be validated through a market research. It involves a fact-finding research on the appetite of the masses, readiness of the stakeholders (Legal, Regulatory, Shariah, etc.), end-to-end supply and demand market intelligence for the proposed model.
INTRODUCTION

Technology has no religion. As long as technology is utilized to benefit the humankind, from a Shariah perspective, there is no issue in using it. Zakat is the third pillar of Islam and to enhance the processes and procedures involved in it, technology has been used. The digitization process of zakat has taken place and today we are moving towards digitalization of it. The process of zakat is simple. The Muslim or any person professing the religion of Islam who is eligible to pay zakat could do so to Baitul-mal or directly to any of the categories of asnaf stated in the Quran:

“Zakat is for the poor and the needy, and amil (those employed to administer the funds), for the muallaf (those who have embraced Islam), for in bondage and in debt, in the cause of Allah and for the wayfarer: (thus is it) ordained by Allah and Allah is full of knowledge and wisdom”

(Surah At-Taubah: 60)
If the zakat money is paid to the baitul mal, it is the responsibility of the baitul mal to distribute the zakat money to the categories of asnaf stated in Quran. The latter process involves collection and disbursement and over the years, a number of challenges have been faced in the process of zakat collection and disbursements resulting in employment of various types of technology to overcome or mitigate these challenges.

Some perceive that since Zakat is the third pillar of Islam, there is no work required to convince the payers to pay it every year as they believe that the process of Zakat payment for the payer’s perspective is automatic. Unfortunately, like all the other religious obligations, Zakat has also become complicated and depending on the jurisdiction, there is a need to create awareness among the eligible payers and considering the tax system adopted in the jurisdiction, Zakat collection process has become cumbersome as well. Furthermore, the payment of physical fiat money over the counter to the mosques or other religious offices seems to be outdated and cheques have been used to pay Zakat which has further advanced with the advent of electronic payment systems where online transfer has been adopted. Furthermore, via mobile phones using Unstructured Supplementary Service Data (USSD) code also zakat payment has been introduced in some countries. With Industrial 4.0, the debate of using cryptocurrencies to pay Zakat has also emerged and in fact, in May 2018, it was announced that Blossom Finance in Indonesia has collected Zakat using cryptocurrency (Blossom, 2018) and in May 2020 it was announced that Global-Sadaqah is going to allow Zakat payment using Bitcoin (FinTech News Malaysia, 2020). Furthermore, even those Muslims holding Bitcoins for a year and who reach nisab of Zakat were also made aware of their obligations to pay Zakat on Bitcoins they hold too (Global Ethical Banking, 2020).

In distribution of Zakat, though the categories of asnaf is known from the Quran, the challenge is to find them in real world and verify that they fall within the category and to ensure that they are the ones who really deserve Zakat. Thought Zakat is supposed to be distributed yearly, if the disbursement process is not efficient, then there will be left over of Zakat money that needs to be carried over to the next year. In this regard, there is also need to collect data on how zakat money is used by the recipients to understand how Zakat money is spent to further improvise the disbursement functions which could not be collected without the use of technology.
The typical manual disbursements of physical money does not allow to capture data on how Zakat money is spent by the recipients and as such, different Zakat programs focusing on different aspects of the recipients are introduced. For instance, Majlis Ugama Islam Singapura (MUIS) have Zakat based monthly cash assistance program, settlement of debt program, emergency assistance program, Burial expenses program, study grants program and Fidyah food vouchers program (MUIS, n.d.). Furthermore, the potential of using digital wallets in zakat payment (Salleh et al., 2019) and disbursement has also been explored and the employment of blockchain technology to ensure that zakat payment and disbursement process is transparent is also being explored (Salleh et al., 2019). Rice ATM Machines have also been used to ensure that the Zakat recipients are being able to receive zakat money in a transparent and timely manner (Muneeza, 2019 and Muneeza and Nadwi, 2019).

**ATTRIBUTES OF CRYPTO ZAKAT**

CryptoZakat can be defined as an Ethereum platform where blockchain technology is used to facilitate Zakat contributions that offers an alternative solution, with decentralized and direct transactions that may assist Zakat organizations to receive Zakat money and disburse it to the specified recipients efficiently. This platform ensures that all processes involved in Zakat will be automated and it would be a one stop platform. There are three functions provided in the platform. They are: Zakat collection, Zakat distribution and registration and verification of Zakat recipients.

The owner of this platform could be a registered information technology firm and the service will be provided in affiliation with a regulatory authority or organization that deals with zakat management. Below are the functions of the crypto Zakat platform explained.

**Zakat Collection**

For an individual or an organisation who wishes to pay Zakat, will have to first create a digital wallet in the platform with two currency options: that is either using fiat money or cryptocurrency. E-KYC requirements will be fulfilled in opening the digital wallet. The Zakat money which the individual wishes to pay will be transferred via the digital wallet directly to the recipient’s digital wallet. Therefore, the Zakat payer will have to choose the recipient he/she/it desires and will have to pay the Zakat payment in real time to the digital wallet of the recipient itself. There is no intermediary that will handle the disbursement. To ensure that there is no duplication of recipients in receiving Zakat money in a particular year, the moment the Zakat money is given to a recipient, the platform will automatically oust him to be as an eligible person to receive Zakat in that particular year. In case, if there is no recipient left to be given in that particular year, the system will automatically start to show all the recipients registered for that year and the process will start. However, this would be subject to Shariah approval. This will only happen in a very exceptional situation as today, the recipients of Zakat is increasing and COVID-19 pandemic has turned back the poverty clock.

**Zakat Distribution**

In the crypto Zakat platform, Zakat distribution will be made instantly in real time by the Zakat payer. As such, no time or money will be wasted in giving the money to the recipient.
This will ensure that there is no carry forward Zakat money to the next year and as such, this could be considered as a more shariah compliant way as no back log of Zakat disbursements will be pending. Since all the Zakat recipients who are registered are verified and the transactions are made in the platform, there is no issue of lack of trust or confidence that would arise. Using the digital agreements or smart contracts, the parties ensure that the terms and conditions agreed between the parties are adhered and no time is wasted in execution of the agreements between the parties too.

**Registration and Verification of Zakat Recipients**

A vigilant process involving human resources will be required for this process of registration and verification of Zakat recipients. Since Zakat collection and disbursement will not involve human resources as those two processes are automated in the platform, more effort could be put by the Zakat management organization to focus on finding the Zakat recipients by auditing the applicants and verifying them. Once they are verified and confirmed as an eligible Zakat recipient, they will be listed under a designated Zakat assistance program with background information including history of the person using Zakat money in the past. Every year, the Zakat organization will have to update and verify these information and crypto Zakat will change the function of Zakat organisation as agencies who vigilantly look for eligible recipients of Zakat and the rest of the classical functions they used to perform become extinct. Therefore, Zakat organisations can spend more time and money on creating awareness about Zakat and finding the most deserved Zakat recipients.

The impact of crypto Zakat on the responsibilities of Zakat organizations is huge. Classically, the Zakat organizations are expected to deal manually with Zakat collection, disbursement, registration of zat recipients and verifying them, coming up with programs and creating awareness about Zakat.
Furthermore, they are also expected to manage the zakat fund where all money paid as Zakat is fund collected in one fund and then from that fund disbursements are made to the Zakat recipients. Depending on the efficiency of the Zakat organization in disbursing the funds, often it is impossible to spend all money collected on that particular year to the recipients. This situation forces Zakat organizations to carry forward the money collected to the subsequent year.

However, when crypto Zakat is implemented, the platform automates the process of Zakat collection and disbursement in real time ensuring that there is no need to create the Zakat fund. Furthermore, crypto Zakat enables Zakat organizations to divert its human resources and three main responsibilities; namely in registration and verification of Zakat recipients, creating awareness to boost zakat payers and on how to use crypto Zakat and finally in formulating the Zakat programs based on the need with proper Shariah consultations. As such, with crypto Zakat, zakat administration becomes more transparent and trusted and there will be no unutilized Zakat funds provided that the system is updated and managed properly. The overall effect of crypto Zakat is illustrated in Figure 1 below.

**Classical Responsibilities of Zakat Organizations**

<table>
<thead>
<tr>
<th>Zakat Collection</th>
<th>Zakat Disbursement</th>
<th>Managing Zakat Fund</th>
<th>Registration of Zakat Recipients</th>
<th>Creating Awareness</th>
<th>Forming Zakat Programs with Shariah Consultation</th>
</tr>
</thead>
</table>

**Responsibilities of Zakat Organizations after Adoption of Crypto Zakat**

<table>
<thead>
<tr>
<th>Registration of Zakat Recipients</th>
<th>Creating Awareness of Zakat</th>
<th>Forming the Zakat Programs with Shariah Consultation</th>
</tr>
</thead>
</table>

**Figure 1: The Effect of Crypto Zakat in a Nutshell**
OPPORTUNITIES AND CHALLENGES

The opportunities created by Crypto Zakat is enormous as it enables to have Zakat process to be more transparent in a decentralised manner using digital agreements in a cheap way. Since each and every transaction made whether it is a payment or disbursement of Zakat can be traced via blockchain, the confidence in the Zakat administration system for all stakeholders will increase as the level of public accountability and governance is strengthened. The decentralization way of operation does not require a single regulatory authority or the transaction to be within domestic jurisdiction as allowing cross-border Zakat transaction to increase. Involvement of digital agreements or smart contracts in the process ensure that there is no alteration in the initial agreement made between the parties to the transaction giving the assurance that the original form of the contract remains as approved by all members. Since the automation of processes is easy to happen in crypto Zakat, there are less intermediaries involved decreasing transaction cost to collect and disburse Zakat. As such, human resources of the Zakat organizations could be used in creating awareness and finding the most deserved Zakat recipients. Furthermore, this way the time and money could be used to come up with innovative and effective Zakat programs for the recipients with consultation of the Shariah consultation.

With all the opportunities which crypto Zakat creates, there are also some challenges that would be faced in the implementation of it. No technology can create instant magic and in this regard blockchain technology is also no exception. Rules and regulation to operate crypto Zakat is required to ensure that all parties or stakeholders in the transaction is protected.

Proper governance and information technology related laws need to be put in place and there is also need to invest on the required technology. For this, political will is required in those countries who manage Zakat in a centralised manner while in those jurisdictions where non-governmental organizations manages it needs to take care of the investment part. Shariah rules also need to be agreed beforehand so that the system of crypto Zakat will enable those rules to be reflected in the platform to ensure that there is no Shariah breach or shariah non-compliance risk involved in any stage of the transaction.

CONCLUSION

Zakat is the third pillar of Islam. To ensure that Zakat is managed in the most efficient manner, it is important to utilize the available technology to enhance it. As explored in this paper, there is potential to introduce Crypto Zakat in a sustainable manner.
Upon adoption and implementation of crypto Zakat, the classical role of Zakat organisations will be changed as Zakat collection and disbursement would be automated using the platform and the only concern of the Zakat organizations would be to create awareness about zakat and registering, verifying and updating the most deserved Zakat recipients. Furthermore, they will also concentrate on creating Zakat programs where rules of those programs will be determined to distribute the recipients accordingly. Crypto Zakat will definitely bring a revolutionary change to Zakat collection and payment as no human involvement will be required and the process becomes transparent. It is anticipated that in future Zakat organizations will consider having a crypto Zakat platform building trust and confidence to the administration of Zakat by boosting the integrity of it.

References
My Islamic fintech journey started in late 2016 in the crowdfunding space right after my graduation from INCEIF with a Master of Science in Islamic Finance. Back then, crowdfunding was still a new term that very few had heard of. As I was a member of the INCEIF Student Representative Council, in early 2016 we organized the first fintech talk on campus. We invited EthisCrowd to share their journey of creating the first shariah compliant real-estate crowdfunding investment platform. The lecture hall was full house, and the talk sparked great interest among students and faculty members.

Right after that talk, I had a casual conversation with a colleague of mine to start a similar concept in South Africa where there was a significant finance gap and where this concept would have a measurable social impact. It would also expand the range of shariah compliant investment options for the South African Muslim population. The idea opened my eyes to these new possibilities, and we started exploring ways to establish it. We decided to learn from the EthisCrowd experience, use their brand to build upon their expertise, and to help in scaling one of the first Islamic fintech startups in the world.
In order to help EthisAfrica, I decided to join EthisCrowd office in Kuala Lumpur where I had an incredible experience in a young, passionate, and talented team. I engaged fully with the thriving company, and in less than a year, I feel I gained at least 3-years worth of experience. The learning curve in a fresh start-up is steep and I benefited from wearing multiple hats, being pushed out of my comfort zone, being in such an innovative and delivery focussed environment.

Later in June 2017, I joined EthisAfrica to start working on the implementation, screening of projects and marketing of the first Islamic investment crowdfunding solution in South Africa (probably the first on the continent). We started small with Friends and Family (F&F) seed capital and a handful of team players. Access to capital and lack of regulation were the biggest hurdles to sustain the business.

The first crowdfunding campaign was an immense success. Through Mudarabah investment, investors funded an Early Childhood Development Center that was delivered on time with positive returns for investors. Unfortunately, EthisAfrica’s journey came to a halt because of lack of funding. On top of which, the absence of crowdfunding regulation that would protect the interests of investors, project owners, and the crowdfunding platform made it more difficult to source profitable projects without compromising investors’ interests.

Going back to the core team I started my career with, I joined a dear revert brother who had come from the UK to Malaysia to venture into the Shariah compliant start-up space. In late 2017, we took the reigns of WaqfWorld, a Waqf-related venture that had long been on the shelves. The idea was to build a global cash waqf fund through crowdfunding that would be invested in a shariah-compliant portfolio. Part of the profits were going to be reinvested to sustain the business while the other part was going to finance social and philanthropic projects. The aim was big and so was our vision. The idea was welcomed by most of the partners we reached out to, both in Malaysia and outside Malaysia. However, the challenge of bootstrapping such a big vision with limited funding and the stiff regulation of the Waqf sector didn’t allow the project to come to fruition. However, I am reliably told that a new iteration is in process so watch this space! In August 2018, I joined Elmangos, a thriving start-up driven by the mission of empowering Muslim youth and advance the Islamic economy through business facilitation and robust partnerships.
Through events’ organization, Elmangos launched three flagship events for the industry: the Global Islamic Economy Entrepreneurship Convention (GIEEC), Global Islamic Fintech Summit (GIFS) and Islamic Digital Economy Experience (IDEX). This experience was key to giving me a different angle of exposure to the growing industry and deeper ecosystem connections both inside and outside Malaysia. In the couple of years I was with Elmangos, we noticed the importance of an established and interconnected ecosystem, the evolving market awareness for Islamic fintech products, the readiness of different markets, and the challenges hindering the industry from reaching its full potential.

In early 2020, I joined IslamicMarkets.com, an award-winning Islamic fintech company, with the mission of bringing the fragmented Islamic economy to one platform and in connecting stakeholders to grow and advance the industry. This unique platform provides Islamic economy market insights, industry-led learning programmes, leadership live sessions and masterclasses, and a collaborative messenger tool connecting markets worldwide. In this company, I had witnessed how Islamic fintech solutions have evolved following the unprecedented Covid-19 pandemic. The importance of digital platforms for the industry is becoming more apparent to address the rapid changes of markets and customers’ behaviour by providing timely solutions. This 5-year roller-coaster ride in the Islamic fintech space and hands-on experience has given me a unique lens to be able to view the major strengths and weaknesses of this promising industry:

<table>
<thead>
<tr>
<th>WEAKNESSES</th>
<th>STRENGTHS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Lack of funding:</strong> The sector still needs resources to be mobilised from angel investors, VCs, PEs and the private sector. There remain cultural impediments to supporting new ‘high risk’ ventures which is preventing the much needed flow of capital. Young entrepreneurs have the ideas and the will but the biggest limit to success is the lack of financial supporters.</td>
<td><strong>Niyya (intention):</strong> In my personal experience, the first thing that stands out in Islamic fintech startups’ founders are their sincere intention and passion about adding value and benefit the “ummah”.</td>
</tr>
<tr>
<td><strong>Absence/lack of regulation:</strong> A sound and flexible regulation for this industry will instil more confidence and ensure protection of stakeholders (investors, clients, employees, etc). Stiffness and lack of regulation were among the main reasons many promising ventures had to close or abandon the idea.</td>
<td><strong>Dedication and support by cross-industry players:</strong> The spirit and power of Niyya contributed in forging many partnerships in the industry. Many business owners helped and got help for the sake of helping each other in doing good for the “ummah” and growing the industry for the benefit of all.</td>
</tr>
<tr>
<td><strong>Ecosystem support:</strong> Incubators, accelerators, government dedicated agencies, as well as private institutions such as Islamic banks, are key to nurturing and feeding the industry’s development.</td>
<td><strong>Countries that are driving the industry and serving as a role model:</strong> Countries like Malaysia, UAE and Indonesia were proactive in embracing digital transformation and fintech, hence laying down the infrastructure for the industry to grow.</td>
</tr>
<tr>
<td><strong>Talent and skills:</strong> There is a huge need to upgrade workers’ and graduates’ skills, and attract foreign talent. Soft skills, entrepreneurial thinking, growth mindsets, grit are all highly prized and typically lacking.</td>
<td><strong>Growing market and abundance of opportunities:</strong> The halal economy is worth more than USD6 trillion1 and the Muslim population hovers around 2 billion and growing. This burgeoning market creates a plethora of opportunities to seize and leverage the power of technology in response to this substantial potential demand.</td>
</tr>
<tr>
<td><strong>Governance:</strong> When it comes to governance, the advantages of the start-up space can become its disadvantages. A number of governance issues and examples of poor management practices caused clients to lose trust in certain products/services thus impeding the growth of businesses in this industry.</td>
<td><strong>No specific agenda:</strong> There is no clear or specific agenda for Islamic fintech to serve as a blueprint and measure the industry’s progress.</td>
</tr>
</tbody>
</table>

Note: The Islamic Fintech industry weaknesses and strengths are on the global level. While some countries are faring relatively well compared to others, there is still much room for improvement in the areas they remain weak in.
It is no surprise that my journey started and is still going in Malaysia, the leader of the Islamic fintech industry. Malaysia has established itself as a global Islamic fintech hub thanks to its supportive and comprehensive ecosystem. The leaders’ vision in accelerating technology adoption, a tech-savvy nation, flexible regulation, and incentives to attract investment and talents were the key ingredients in Malaysia’s Islamic fintech development.

Since 2016, the industry has grown by leaps and bounds with more fintech start-ups sprouting in new countries and becoming more balanced in terms of the verticals served. While crowdfunding was the dominant field in 2017 with 35% industry share, today it represents less than 20% with more verticals rising such as blockchain & cryptocurrency, data & analytics, roboadvisory, and digital banks.

In my opinion, the way forward for the industry is to align with sustainability and SDGs. Successful businesses are the ones that solve a problem, and what is more arduous today than social, climate and environmental issues? Furthermore, young generations tend to connect more with businesses with stories and the passion to make a difference. Islamic fintech should go beyond the simple product/service model and focus on serving, not only Muslims, but the wider world through technology and Islamic principles. Last, being “Islamic” or “Shariah-compliant” alone is not sufficient, customer experience and storytelling are key to define success from failure.

3. MDEC FinTech Report 2019
champion
/'tʃæmpɪən/

INCEIF MBA
(Sustainable Business)
aims to build Champions
of sustainability for the
future

• MBA
(Sustainable Business)

The Search for Sustainable Business Champion is ON

INCEIF is a leader of sustainable industry advancement. With conscientious knowledge sharing, we empower learners to hone their strengths and achieve professional success, while instilling strong ethics and solid values.

Our MBA (Sustainable Business) programme will enable you to foster sustainability in business and within your community at the grass-roots level, while enriching your professional development and allowing you to realise your leadership potential. Designed by a world class consortium of seasoned industry experts, this programme imparts comprehensive knowledge and Action Based Learning in multiple core areas, including Sustainability Management and Investment, Ethics and Professionalism, and Social Finance.

Today’s dream can be tomorrow’s reality.

Think you have what it takes or know someone who can be a Sustainable Business Champion? Nominate now at www.inceif.org/MBA or email their details to marketing@inceif.org today!

Intakes in Jan • June • Sept

marketing@inceif.org
www.inceif.org/MBA
facebook | twitter | linkedin | youtube | instagram | @INCEIF

INCEIF
THE GLOBAL UNIVERSITY OF ISLAMIC FINANCE

AACSB ACCREDITED
5 YEAR 2017-2022
INCEIF SCHOLARSHIPS

We believe in a world of unlimited opportunity for those with talent, drive, confidence and ambition.

YOUR FUTURE SUCCESS STARTS HERE.

- PRESIDENT’S SCHOLARSHIP
- CHANCELLOR’S SCHOLARSHIP
- SPECIAL BURSARY
- KHAZANAH-INCEIF SCHOLARSHIP
- MALAYSIAN INTERNATIONAL SCHOLARSHIP (MIS)

WHY INCEIF?

WORLD CLASS
INCEIF is the first Islamic finance university in the world to be accredited by AACSB (Association to Advance Collegiate Schools of Business), placing us among the top 6% of business schools, globally.

PROVEN
Our SETARA 5 rating makes us one of Malaysia’s premier universities.

INTERNATIONAL
With alumni from over 70 countries, INCEIF enjoys an international presence in a wide range of fields.

AWARDS
Since 2015, INCEIF’s research has earned the university a position as one of the top five among Malaysian higher education institutions in the Research Papers in Economics (RePec) rankings. In Asia, INCEIF has consistently remained on the Top 100 RePec list.

PRACTICAL
Our curriculum is driven by issues relating to innovation and leadership within the industry, bridging the gap between the theories propounded by academia and the practical operation of industry players.

Connect with us at
Facebook
Twitter
LinkedIn
YouTube
Instagram
@INCEIF

www.inceif.org
marketing@inceif.org
+603-7651 4000
THE ROLE OF ISLAMIC FINANCE IN THE COVID-19 PANDEMIC